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**Is China still socialist?
A Marxist critique of János Kornai's analysis of China**

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Is China still socialist?
A Marxist critique of János Kornai's analysis of
China

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Abstract

This thesis investigates if China's system conforms to János Kornai's theory of reform socialism. To facilitate this study Kornai's theory of socialism is outlined in depth and its basic features are compared with evidence drawn from a broad range of multidisciplinary research on contemporary China. I find that the three necessary and sufficient features of socialism that Kornai identifies are all present. I also reveal other similarities between reform socialism and China's contemporary system.

The idea that China is best understood as a variety of capitalism is considered, and I reflect on the dynamics of the state and private sector in modern China. After 1978 an important inspiration for China's economic reforms was the Soviet New Economic Policy (NEP) introduced under Lenin in 1921. The Soviet economist Evgeny Preobrazensky studied the forces shaping policy during the NEP and elaborated a Marxist method to reveal how the contradictions between socialist and capitalist tendencies vie for dominance over the economy. He views this economic conflict as a type of class struggle, which takes the form of 'primitive socialist accumulation' (PSA). The planned development of the economy accumulates from the private sector, and increases the importance of the working class in the economy.

The state sector exercises its dominance by exploiting its semi-monopolistic power and undertakes projects of vast scale and ambition. The workforce finds it is able to exert considerable pressure on the ruling Party and bureaucracy. This indicates that the relationship between the working class and the Party and state remains central to the power relations governing Chinese society today.

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Abbreviations

Abbreviation	Meaning
ACFTU	All China Federation of Trade Unions
AMCs	Asset Management Companies
CCP	Chinese Communist Party
CMC	Centrally Managed Capitalism
CMEs	Co-ordinated Market Economies
CSOEs	Central State Owned Enterprises
FDI	Foreign Direct Investment
FYP	Five Year Plan
HBC	Hard Budget Constraint
LMEs	Liberal Market Economies
MofCOM	Ministry of Commerce
NBS	National Bureau of Statistics (China)
NDRC	National Reform and Development Commission
NEP	New Economic Policy (Soviet Union 1921-1928)
PSA	Primitive Socialist Accumulation
SASAC	State Owned Assets and Supervisory Commission
SBC	Soft Budget Constraint
SOEs	State Owned Enterprises
VOC	Varieties of Capitalism

1. Introduction

1.2. Context

1.2.1. *Personal background*

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1.3. Conceptual framework: theories and methodology

1.3.1. *Preobrazhensky's Marxist framework and method*

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1.4. Chapter Outlines

There is a broad global consensus in academia, politics, and economics, as well as among the wider public, that China's system represents an enigma. Some scholars have described it as a repressive and barbaric form of capitalism (Andreas, 2008; Hurst, 2013; Harvey, 2011). Others, such as Joshua Cooper Ramo (2004), have suggested that a 'Beijing Consensus' is replacing the 'Washington Consensus' with a new model of capitalism. The late Giovanni Arrighi (2009) suggested that China is trailblazing a new model of East Asian development, with a huge appeal to the Global South. In a similar vein, the former Chief Economist and Senior Vice President of the World Bank, Lin Yifu believes that China's economic miracle is based on a growth formula that other developing countries can emulate (Lin et al., 2003; Lin, 2012; Banque mondiale and Commission on Growth and Development, 2008).

China's idiosyncratic status is rooted in the fact that after socialist states in Europe and the former Soviet Union collapsed China's system not only survived but also flourished. The year 1989 marked a dramatic turning point in world history: social protests erupted, and in most of these socialist states a process of internal disintegration of state power began. Furthermore, it was in Beijing that this year of street demonstrations, rallies and revolutions that shook socialist states began. Students initiated this movement. It protested against corruption and inflation, and won widespread support amongst the urban masses. On 4 June the army forcefully seized back control of Tiananmen Square, the epicentre of the unrest, and the movement was defeated.

The movement that erupted in East Germany demanded political change. This led to the breaching of the Berlin Wall on 9 November 1989. Then, huge protests broke out across Eastern Europe, which brought down socialist governments in Czechoslovakia, Bulgaria, Hungary and Romania. In the former Soviet Union, Mikhail Gorbachev, the Communist Party's leader since 1985, had initiated reforms from above, based on 'glasnost'. This term signified openness of discussion, which was combined with economic restructuring. However, economic reforms stoked up social tension and increased inequality, and this intensified popular unrest. In the summer of 1991 the Soviet Union collapsed following an aborted coup. The Cold War was over. Socialism lost. Capitalism won. Or, so it seemed.

However, nearly 29 years after the dramatic events of 1989 China's Communist Party remains firmly in power. Why did it survive and flourish when Eastern Europe and the Soviet Union collapsed? This question has perplexed and intrigued me since 1989. It was the fall of the Berlin wall that led me to engage with questions of the role of markets in a socialist system and the complexities of the process of economic transition from capitalism to socialism.

1.1. Research question

This thesis poses the question is China still socialist? This assumes that China was once socialist, but what are the defining characteristics of this lost world of socialism? If China is no longer socialist, is it a variety of capitalism? How well does China system match-up with theories of Chinese capitalism? And how influential are China's socialist remnants? Does China's combination of capitalism and socialism represent a new system of political economy, in which markets and planning are but neutral methods of economic progress?

To address these questions, I draw on the analysis of socialism worked out by the Hungarian economist János Kornai, which provides the pivotal reference point around which this thesis revolves. His theory exercises a

towering influence in the field of the political economy of 20th century socialist systems. His ideas were also central to Chinese policy debates on economic reform from 1985 onwards. In the context of this thesis, his definition of socialism will be used to evaluate its relevance to China today.

I also engage in a historical analysis of the Soviet Union in the 1920s. Kornai describes this period as the *prototype* of all future socialist systems. I survey the terrain in which debates on the transition from socialism to capitalism took place. This was an environment where the state and private economy were both present and influential. Does China's combination of a dominant state sector surrounded by capitalist and pre-capitalist economic forms reveal parallels to the circumstances in the first decade of the Soviet Union? If so, what are these parallels? To address these questions, I analyze China's economic structure, economic debates, and internal dynamics, by comparison with the Soviet system during the New Economic Policy (NEP) from 1921 to 1928. My questions are concerned with examining the main contradictions and driving forces of the New Economic Policy, as well as the main regulators of the economy.

The work of the leading Soviet economist Evgeny Preobrazensky is crucial to such a historical comparison. His theory of primitive socialist accumulation was developed most fully in his study of the New Economic Policy. I ask what insight his theory can provide about Chinese economic debates and policies?

Even though both Kornai's and Preobrazensky's theories of socialism are highly respected by specialists in the field of socialist economics, their value for the study of China's political economy has been neglected in English language scholarship on China.

Social relations of power and class are central to the concerns of both thinkers and they lie at the heart of the Marxist theory of social change. To expand on their study of the political economy of socialism and capitalism, I attempt to supplement their insights with an exploration of

China's modern class relations. This concentrates on the role of the working class in China's transformation. To this end, I examine the formation of the working class as an objective and a subjective force. To assist in this task I employ concepts of class and state power championed by the prominent American sociologist Eric Olin Wright (1994, 2000a). I reflect on what insight this type of class analysis can elicit about the enigmatic features of China's system.

1.2. Context

1.2.1. Personal background

My interest in the fate of socialist states comes from personal experiences in 1989. This sustained my on-going fascination with socialism, communism and Marxism, and inspired my focus on China. My mother is German and my father is Chinese Malaysian. As a consequence, when I became interested in Marxism in 1980, East Germany and the People's Republic of China presented fascinating and intriguing questions that I still find challenging and exciting today. Studying Marxism, inevitably involved dealing with the question of how to evaluate the Soviet Union and other states, which claimed the socialist and Marxist mantle as the philosophy guiding their principles and state system. Discussions around this question seem to me to lie at the heart of any serious attempt to propagate, explain and formulate an alternative to capitalism that might also have a popular appeal in the advanced capitalist countries.

In the summer of 1988 I moved from London to West Berlin in order to regularly visit East Berlin. I hoped to gain a better understanding of the system, to make contact with like-minded people in East Germany, and to participate in what I hoped would become the revolutionary transformation of East Germany and of all the Eastern bloc countries towards a form of socialist democracy. In the summer of 1989 I enrolled to study at the Humboldt University in East Berlin. There I worked with

like-minded students and opposition activists to form independent organs of student representation and I co-authored a Marxist opposition manifesto in October 1989. I witnessed first hand the beginnings of the mass social unrest against the Party and state and joined protest demonstrations in Berlin and Leipzig throughout October and early November. On the morning of November 10th I climbed on top of the Berlin wall at the Brandenburg Gate.

At that time, I wrote articles advocating the democratization of power and the defense of public property. I hoped and imagined that Stalinist rule would give way to a socialist democracy based on workers' councils, and that such a political revolution would retain public ownership and planning whilst simultaneously democratizing the state.

Although these ideas seemed to be well received at the start of November 1989, after the Berlin Wall was open, German reunification soon became the central idea that gripped the minds of the masses and became a material force. On demonstrations in Leipzig I witnessed protestors sing the communist anthem 'The Internationale' with one breath, and then chant 'Germany one fatherland' with the next. By December, a sea of West German flags fluttered in the wind, and the German national anthem echoed on the streets.

When the Berlin Wall was opened millions of East Germans engaged in a mass comparison of systems. This was judged by the quality and availability of consumer goods and services, as well as by individual and political freedoms. East German claims to systemic superiority turned to dust. Indeed, almost everything produced in East Germany's socialist system was in shorter supply and of inferior quality to those made by West German capitalism. Popular moods and ideas changed rapidly, but the dominant feature was symbolized by an urgency to acquire West German currency to buy the newly accessible goods from the West. The slogan 'if the West Mark doesn't come to us, we will go to the West Mark' forced the hand of the chancellor Helmut Kohl. Either West Germany would provide access to Western currency or millions of East Germans

would just move to the West. Kohl grasped this opportunity to call for rapid national unification through the assimilation of East Germany by the West German Federal Republic.

When Germany reunified I left Berlin for China in October 1990 and I worked teaching English in Shanghai for a year and a half. Many of the same problems of low quality and the poor availability of goods existed there too. There were ration cards for some basic foods and for cooking oil. However, private incentive and investment was permitted to operate within the framework of the socialist system on a much broader scale than had been the case in East Germany. Street markets flourished, and private shops and restaurants were commonplace. Kentucky Fried Chicken had an outlet in Shanghai, something that would have been unthinkable in East Germany, and the difference between the local currency and the convertible foreign exchange currency was not very large. Shops were well stocked and shopping streets in Beijing and Shanghai were bustling market places, very different to the atmosphere in Eastern Europe or the USSR.

I became increasingly interested in the question of the balance within a socialist economy between planning and markets, and between public and private ownership forms. These issues had been 'resolved' in East Germany by building the Berlin Wall in 1961, but they returned with a vengeance to sweep away the East German system like a Tsunami when the Wall was breached on 9 November 1989.

1.2.2. Historical background

János Kornai maintains that his systems theory derives from a tradition that seeks to define the basic features of a socio-economic system. This intellectual trend can be traced back to Karl Marx. In *Capital* Marx applies this method to study the emergence, ascendance, and predicted demise and overthrow of the capitalist mode of production and its replacement by socialism. Marx expressed the view that the natural laws of capitalism meant that: 'The country that is more developed industrially only shows,

to the less developed, the image of its own future.’ (Marx, 1990, p. 91 [1867])

In 1881, when Russian revolutionaries tried to work out how to apply Marx’s theory to their country, one of their number, Vera Zasulich, famously asked Marx’s opinion on the fate of ancient communal property forms in the villages, and whether they must submit to capitalist relations. Marx replied in the negative.¹ However, as Russia remained economically backward compared to Western Europe, it was commonly accepted amongst Russian Marxists that the character and prospects of a future Russian revolution would be circumscribed by the limited development of the productive forces. The predicted revolution would take a bourgeois or capitalist form, and this would lay the material and political foundations for a future socialist revolution.² However, Leon Trotsky suggested that the constellation of class forces in Russian society meant that the Russian bourgeoisie was too weak and vacillating to take the lead in society, and so, the working class would assume the leading role in the forthcoming revolution, which would combine bourgeois and socialist tasks (Trotsky, 2007 [1931]). In the 1920s, analogous debates to those in Russia occurred among Chinese Marxists when discussing the possibilities and character of the Chinese revolution (Schwartz, 1954).

Karl Marx employed a concept of Chinese history that lacked the depth of his analysis of Russian society. His theory of Chinese society proposed that an Asiatic mode of production dominated Chinese society rather than feudalism (Wittfogel, 1962a, 1962b). Since then, our understanding of Marxist concepts of modes of production and exploitation has advanced with more sophisticated research into Chinese and Indian history. In particular, Jairus Banaji’s analysis redefined these historical systems as a ‘tributary mode of production’.³

Joseph Needham initiated a profound and wide-ranging scientific debate about China’s place in world history before the ascendance of Western capitalism (Needham and Wang, 1964). His question, known as the

Needham Puzzle, asked why modern science failed to originate in China. His own conclusion was that China's social relations had hindered its development. His research completely changed our understanding of the position of China in world history and it underpins a fascinating field of scientific, economic and cultural analysis (Lin, 1995; Brook and Blue, 1999; Pomeranz, 2001; Needham et al., 2004; Chun, 2013).

When Marxist ideas first gained adherents in China, Li Dazhao, the co-founder of the Communist Party, immediately grasped the significance of historical theory for the revolution. In 1918 he wrote: 'If one can write the history of billions of people, then one can have the authority to move the minds of billions of people.' (Brook and Blue, 1999, p. 131)

Analysis of the basic character of China's social system has exercised a profound influence on the political and economic policies of the Chinese Communist Party since it was founded in 1921. Debates about the dominant mode of production in China played a pivotal role in the fate of the Chinese Communist Party throughout the 1920s. This mattered to the Party because its theoretical analysis formed the basis of its tactical and strategic orientation. Indeed, up to today, the way that the Party defines the social system continues to shape its policies to correspond with its official characterization of the epoch.

In the 1920s the party debate on China's system revolved around the question whether China was dominated by feudalism. If it was, the task of the Party was to prepare for a bourgeois-democratic revolution. However, if capitalism already dominated China, then a socialist revolution would be an immediate objective. These Marxist debates about China revisited questions raised in the Russian revolution, where despite the backward state of the productive forces, the constellation of class forces helped the Party to seize state power in 1917. If China were similar to Russia, the Chinese Party should have maintained its organizational independence from the capitalist Nationalist Party, known as the Guomindang (Wang, 1980; Benton, 1996; Trotsky et al., 2006).

However, by the end of the period 1921-1927, the view that China was dominated by a pre-capitalist social formation won the day. The Chinese Communist Party and the Communist International agreed that the Communists should subordinate themselves to the Nationalists. Chiang Kai-shek, the leader of the Guomindang, made use of this situation to strike a crushing blow to their urban revolutionary cadre in Shanghai in 1927 (Issacs, 2015; Trotsky et al., 2006). This drove China's Communists from the cities, and shifted the Party's central locus of struggle from its urban revolutionary roots to the rural hinterlands. These events provided the backdrop for Mao Zedong's reformulation of the tactical and strategic orientation of the Chinese Communist Party, which formed the cadre of a revolutionary army in warfare, and of state power and administration in the liberated zones that it established between 1929-1949 (Benton, 1992).

1.3. Conceptual framework: theories and methodology

This thesis is based on a Marxist theoretical approach, which regards social knowledge and political institutions as being intertwined with the interests of those who control the dominant economic system, and holds that the political superstructure is rooted in its economic base. Marx's study of the economic system of capitalism advanced political economy with his theory of surplus value. It also identifies a tendency to concentration and monopoly, which intensifies the social nature of production and generates the modern working class. Cyclical crises are taken to illustrate the temporal nature of capitalism, which points the way to an alternative – socialism based on rule of the working class. Class struggle is viewed as the means of securing political freedoms and preparing for the overthrow of capitalism.⁴

In *Capital* (1990 [1867]), Marx studied how the core features and driving forces of the capitalist system generate and unleash extraordinarily dynamic capacities to produce, exchange, invent, transform, and revolutionize, science, technology and all human relations. However, the basic contradictions between the workers and the capitalists, and between different capitalists,

simultaneously gives rise to dysfunctionality, boom-bust cycles, and class conflicts.

1.3.1. Preobrazhensky's Marxist framework and method

The Russian economist Evgeny Preobrazhensky plays a central role in the application of Marxism that is adopted in this thesis. He developed a comprehensive and sophisticated theory about the transition from capitalism to socialism in an underdeveloped economy. This drew on the concrete experience of the Soviet Union in the 1920s, to explain the dynamics and contradictions of socialist development in a backward economy.

A close reading of Preobrazhensky's book *The New Economics* (Preobrazhensky, 1965 [1926]) and of his theory of transition to socialism shows how he applied Marxist categories of capitalism and socialism to study the internal dynamics of the Soviet economy during the period of the New Economic Policy (1921-1928), when the Bolshevik regime selectively used market mechanisms to promote economic recovery.

Deng Xiaoping, the father of China's economic reforms, initiated reform policies by specific reference to Lenin's NEP. China's mix of state ownership and control of the commanding heights of the economy, combined with a sizeable private economy, corresponds to the combination of economic forms that existed during the Soviet NEP (Xu, 2017).

My investigation of Preobrazhensky's theory looks at how his abstract categories, based on pure features of capitalism and socialism, were amended and appeared in real life during the NEP. It explores how the contradictory interplay between the capitalist law of value and socialist planning principles gave rise to the victory of bureaucratic planning under the leadership of Joseph Stalin. By examining the historical circumstances in which this system emerged, it is possible to identify how the Stalinist method of socialist accumulation diverges from Preobrazhensky's original concepts and policy proposals.

In the period governed by primitive socialist accumulation, the methods employed to extract resources from a capitalist enterprise encompass a wide range of possible measures, from mild (a tax on profits), to draconian (expropriation without compensation). The decision as to which of these measures are most suitable is contingent on concrete circumstances.

Preobrazhensky developed his model of primitive socialist accumulation (PSA)⁵ to work out the regularities of economic activity; to understand conflicting social processes, and to develop policies aimed at extending the influence of planning.

He wrote:

‘I devote myself to the modest task of first abstracting from the actual economic policy of the State, which is the resultant of the *struggle* between two systems of economy, and the corresponding classes, so as to investigate in its pure form the movement towards the optimum of primitive socialist accumulation, to discover the operation of the conflicting tendencies, as far as possible in their pure state, and then to try to understand why the resultant in real life proceeds along one particular line and not another.’ (Preobrazhensky, 1965, p. 62)

1.3.2. Contrasting Capitalism and Socialism

Preobrazhensky shows that Karl Marx presented capitalism in a *pure form and as a complete system*, contrasting it with its antecedents and its predicted communist successor to identify the unique characteristics and conditions in which the finished system of capitalism operated; both Marx and Engels avoided utopian visions of socialism and made their forecasts based on their analysis of capitalism.

Preobrazhensky applies Marx’s theory to develop a method to examine the process of economic transition from capitalism to socialism (1965, 1974). He believed that the categories of political economy would be transformed under planned socialist production. The commodity will be replaced by the product; value by labour-time; the market by

bookkeeping of a planned economy; surplus value by surplus product; and social technology - as a science of socially organized production - will replace political economy (Preobrazhensky, 1965, p. 162 [1926]).

This new science would forecast economic necessity and propose how labour and production should be organized to satisfy wants and needs. The study of future impacts would supplant the estimation of consequences; requiring complex regulatory organs of social foresight and planned guidance (Preobrazhensky, 1965, p. 55).

Although Preobrazhensky developed a comprehensive method based on Marxist categories to analyse the process of primitive accumulation in general, his analysis of the state superstructure did not investigate the bureaucratic system of politics and economics that came to reign in these socialist states for most of their existence. This system became entrenched in the Soviet Union, and it was emulated or replicated in its essential features in China and other socialist states.

For his part, Leon Trotsky did examine the rise of the bureaucratic system of socialism that was first consolidated under Stalin. But Trotsky viewed this regime as a betrayal of the revolution and a temporary aberration that would be overthrown with the dawn of new socialist revolutions in the advanced capitalist countries (Trotsky, 1999). In any case, Trotsky was assassinated in 1940 and many new socialist states, including China, were established between 1945 and 1949.

Kornai was able to study the main features of these systems in depth. So I draw on his analysis of socialism, which studies the economic structure, the system of economic coordination, and the superstructure of the state. And I investigate how the state superstructure ensures the reproduction of the system as a whole.

However, his conclusions elevate the classical system of Stalinist socialism and reform socialism to the only possible types of socialism. Indeed, Kornai maintains that because these states were all

dictatorships, democracy and socialism are by definition mutually incompatible (Kornai, 2016).

1.3.3. Kornai's system's theory

Preobrazhensky's theory is based on his analysis of the Soviet Union in the 1920s, whereas Kornai's theory is rooted in his analysis of 20th Century socialist states. Kornai's theoretical insights about reform socialism provide the structure that frames my investigation of the system that operates in China.

Like Preobrazhensky's method; János Kornai's systems theory originates from the Marxist tradition. It identifies the dominant characteristics of a society based on his 'systems theory' method. Kornai, like Marx, believes that socialism and capitalism operate according to fundamentally different laws. So, a comparison between capitalist and socialist systems can generate broad insight into the nature of a given society and its social and economic relations. This framework is used to elicit the patterns, regularities and characteristics of a given social system.

Kornai's theoretical insights about classical and reform socialism provide the structure that frames my overall investigation of contemporary China. The analytical tools he uses to study 20th century socialist states provide detailed explanations for the specific socialist features of China's system.

My study of Kornai's theory focuses on his exposition of basic and fundamental features of socialist systems, with particular attention paid to his concept of reform socialism. I select the three main features of socialism that Kornai uses as definitional determinants of the system and explain their importance to his theory. These are: Communist Party rule with an ideology that is hostile to private property; the dominance of public property in the commanding heights of the economy; and the dominance of bureaucratic coordination of the economy. These three basic foundation stones of Kornai's socialism are the benchmarks used to test whether China's system fits his definition of socialism.

The first feature: Communist Party power and ideology, are concerned with what is seen as the superstructure in Marxist terminology. To study China's state system, I examine articles in the Western and Chinese press, government reports, and the speeches of China's leaders. I also selected pertinent material from academic articles, journals and books on the Chinese Communist Party, its state organs, internal discipline mechanisms, governmental and administrative structures, and governance systems, I and evaluated them with a view to identifying the dominant trends shaping and determining the behaviour and ideas of the Party and state.

It is hoped that by examining China's system through the prism of the theories of Preobrazhensky and Kornai, some new light can be shed on the contradictory interplay of powerful social and economic entities, and the basic forces governing Chinese society.

1.4. Chapter Outlines

This PhD asks the question if China is still socialist. To answer this question I employ two primary and two secondary approaches, which offer different perspectives and frameworks from which to examine the Chinese system. The primary approaches are based on the ideas of János Kornai and Evgeny Preobrazhensky. Kornai's theories of socialism and capitalism, and his analysis of China, act as the macro-level framework structuring the thesis as a whole. Some aspects of his work appear in every chapter.

Two chapters focus on an exposition of the theories of the main thinkers informing my analysis. Chapter 2 explains Kornai's theory of reform socialism in depth. Chapter 3 examines which of its fundamental features are applicable to Chinese reality. Chapter 4 examines a representative sample of theories, which locate China's system as a variant of capitalism. Chapter 5 examines the rise and fall of the Soviet New Economic policy and Preobrazhensky's theory of Primitive Socialist Accumulation. Chapter 6 uses Marxist methods of class analysis to

examine China's system with special reference to the position of the working class. This chapter employs concepts from Erik Olin Wright's theories of class and class conflict to interrogate the nature of Chinese society. Chapter 7 concludes that China's system broadly conforms to Kornai's concept of reform socialism, and that employing Preobrazhensky's theoretical insights can enhance this concept.

Chapter 2

This chapter examines and explains Kornai's theory of socialism in general, and reform socialism in particular. It begins with an investigation of his systems' theory, which isolates the minimal necessary and essential characteristics of socialism in order to distinguish it from capitalism. The focus is placed on three primary foundation stones: rule by a Communist Party that is hostile to private property; public ownership of the dominant sectors of the economy; and bureaucratic coordination of economic activity. A system based on the three fundamental features of socialism will display a tendency to generate patterns and regularities of economic behaviour that merit inclusion as secondary systemic phenomena. However, these appearances are not regarded as definitional characteristics of socialism i.e. they are not necessary and essential to it, and may also occur in capitalist systems. Of these features I focus on the tendency to use 'forced growth' as an instrument to overcome backwardness, and the dynamics, which give rise to this drive within socialist economies. I also look at the regularities of cyclical growth, the interplay of vertical and horizontal relations of power, the budget constraints on enterprises, pressures that give rise to reform and revolution, market socialist experiments, the emergence of the private sector, and its impact on the demise of socialist systems.

Chapter 3

To consider the degree to which reform socialism is a viable designation for China's system, I assess the degree to which Kornai's theory, method, categories and observations are applicable in China today. I

draw on a wide range of Sinological scholarship to evaluate the nature of the CCP's ideology and its system of state power, particularly since 1989. This involves sketching an outline of the CCP's apparatus of political, administrative and state power. The CCP's relationship to the commanding heights of the economy is investigated in some depth, and differences amongst scholars and economists about how to categorize China's ownership forms are explained. The extent of state ownership of the commanding heights is evaluated in the light of these interpretations. Kornai's holistic approach is used to appraise the centrality of the Party's full spectrum of economic and extra-economic instruments that work to sustain and reproduce its dominance under socialism. China's planning system was amended in the 1990s. The new planning process is assessed in the light of these significant changes. The way it functions is gauged by reference to the 12th Five-Year-Plan 2011-2015 and to the ambitious New Urbanization Plan; the advance of the state and the anti-corruption campaign under Xi Jinping also serve to illustrate the direction of China's trajectory.

Chapter 4

Kornai's own assessment of China as a variant of capitalism is evaluated along with a diverse mix of parallel theories of capitalist China. These theories encompass the historical narrative of China's trajectory towards capitalism, institutional comparisons with Germanic and US capitalism, as well as assessments of parallels with developmental state theory and Japanese and East Asian capitalism. These debates on the characteristics of Chinese capitalism return us to the basic problem of defining capitalism.

I reflect on two Marxist theories of capitalist restoration in China, which display a marked tendency to paint the emergence of widespread market activity as being equivalent to the end of planning and the victory of capitalism. In addition, China's achievements in social progress are marginalized within a narrative that is consumed by the compilation of

negative illustrations of the capitalist degeneration of society, producing a rather narrow and skewed assessment of China's system.

An evaluation of the negative impact of state monopolies illustrates the need to consider the positive role that the combined monopolistic economic power of vast interconnected entities affords. To contextualize this, the role of companies that dominate the commanding heights of the modern world economy is evaluated. Similar Chinese companies are identified and the sanctions and responses available to the state to control them are described. Kornai's own theory of capitalism is the subject of the final section of this chapter. His core arguments are expounded with a view to assessing the extent of China's correspondence to this theory. The chapter concludes with Xu Chenggang's appraisal of whether and how Kornai's system corresponds to Chinese reality.

Chapter 5

The Soviet economist Evgeny Preobrazhensky elaborated a Marxist theory of economic development by studying the concrete conditions in the Soviet Union in the 1920s and by contrasting Karl Marx's theory of socialism with this reality. This approach provides a supplementary framework to Kornai's theory of reform socialism. It can be used to weigh up the contradictions and assess the driving forces behind the process of state accumulation in a backward socialist economy. Like the second chapter of this thesis, this involves a detailed exposition of a complex theoretical method. However, I believe that the insights that this intricate exposition provides, penetrates into some of the more mysterious qualities of China's socio-economic system.

The scene is set by reference to the rise and fall of the New Economic Policy in the 1920s. The associated victory of Stalin is contextualized within the framework of the Soviet Industrialization Debate as the product of multiple social impulses pushing towards the ascendance of bureaucratic planning. I conclude by selecting and isolating ten core

macro-level features of Preobrazhensky's theory that I suggest can effectively capture China's macro-level economic processes.

Chapter 6

The working class is the main subject within the Marxist vision of socialism. So it is logical, and probably necessary, to address the role and position of the working class in any discussions about whether China is still socialist. I approach this task by studying the historical development of the working class in the People's Republic as a class in and for itself. To do this, I examine the way that economic policies and plans fostered the formation of the working class in the Maoist period and during the reform era, and I consider a variety of displays of workers' unrest.

To assist this process I employ categories, terms and concepts that the sociologist Erik Olin Wright developed to consider twentieth century class relations. This offers a framework that sheds light on class formation in pre-reform China, which was mainly circumscribed by stifling restrictions on mobility between the town and country and by the dominance of the party and state over the lives of the people.

The reform era generated a far more diverse, complex, unequal and colourful class structure. It engendered capitalist billionaires; a new and relatively affluent social-strata, changes to the social relations in the urban state-owned workplaces, and the influx of an immense new working and semi-working class constituency formed through mass migration.

Social unrest, particularly within the working class is evaluated in relation to the CCP, which has as one of its primary objectives, the maintenance of social stability and the pacification of outbursts of social antagonism. Studies of the key characteristics on display in a variety of social protests in China inform this assessment of the CCP's policies and programme. I suggest that there is a close dialectical relationship between social unrest

and party policies. This is expressed in the party's official theories, in state actions, and in its legal and ideological orientation. This finds reflection in the concealed and overt impact of protest on the party, and in the relationship between the upper and lower levels of state power.

Chapter 7

My conclusions are based on evaluating the general macro-level relevance of Kornai's ideas, both where I agree, and where I disagree with his analysis. I argue that the internal consistency of his reform socialist theoretical model is undermined by his specific analysis of contemporary China. I suggest that Kornai's concept of workers' self-management merits identification within his theory as a systemic specific feature of socialism. I argue that this feature plays an important role in shaping China's system. Furthermore, I suggest that Preobrazhensky's theory of Primitive Socialist Accumulation offers a powerful theoretical tool that can be used to supplement and enhance Kornai's theory of reform socialism. However, if correct, this would mean that socialism is not a system doomed to inevitable collapse, as Kornai believes.

¹ The full correspondence can be found at

<https://www.marxists.org/archive/marx/works/1881/zasulich/index.htm>

² Lenin writes in 1905 'The degree of economic development of Russia (an objective condition) and the degree of class consciousness and organisation of the broad masses of the proletariat (a subjective condition inseparably connected with the objective condition) make the immediate complete emancipation of the working class impossible. Only the most ignorant people can ignore the bourgeois nature of the democratic revolution which is now taking place; only the most naive optimists can forget how little as yet the masses of the workers are informed about the aims of Socialism and about the methods of achieving it. And we are all convinced that the emancipation of the workers can be effected only by the workers themselves; a socialist revolution is out of the question unless the masses become class conscious and organised, trained and educated in open class struggle against the entire bourgeoisie.' <https://www.marxists.org/archive/lenin/works/1905/tactics/ch02.htm>

³ Here, state power is exercised over the means of production and over surplus labour. Banaji finds that these imperial states based on monetary economies displayed considerable dynamism (Banaji, 2013).

⁴ This is based on Lenin's Three Sources and Three Component Parts of Marxism.

<https://www.marxists.org/archive/lenin/works/1913/mar/x01.htm> Accessed 20 Jan 2017

⁵ I believe that the term primitive socialist accumulation should be replaced by 'original' or 'primary' socialist accumulation. This corresponds more closely with the term from Marx, which refers to 'ursprunglicher' accumulation. The translation of 'ursprunglicher' as 'primitive' starkly captured the barbarity of the process of capitalist accumulation. However, 'ursprunglicher' socialist accumulation was supposed to be a progressive and positive process. However, I will employ primitive in this PhD because it is better known and is generally used in the literature.

2. János Kornai's theory of socialism

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- 2.9. Conclusion

2.1. Introduction

As I began to research socialist economics for this PhD, János Kornai's name appeared time and again in the literature. Kornai, born in 1928, is a Hungarian economist who began his intellectual analysis of socialism as a committed Marxist. He became disillusioned with the Hungarian system of planned economy after the repression of the Hungarian revolution of 1956 but continued to work as a professor at the Hungarian Academy of Sciences investigating the socialist system and its flaws. In 1984, he eventually took a post at Harvard University.

Academics and economists from a diverse spectrum of intellectual and normative backgrounds have respected and praised his work for a number of decades. The Hungarian-American sociologist Ivan Szelenyi

considers Kornai to be ‘the most influential scholar of the political economy of state socialism in the world today’ and calls his magnum opus *The Socialist System* ‘the last textbook one needs on the communist economy’. The prominent Sovietologist Alec Nove describes it as ‘a masterly presentation of the nature of the functioning of the Soviet-type system, and an equally masterly explanation of the failure of attempts to reform it’ (Nove, 1993, pp. 1057–1069). The Marxist academic Michael Lebowitz sees Kornai’s book as ‘a political economy of the vanguard mode of production’ which unravels its systemic laws of motion in a similar way that Marx’s *Capital* did with capitalism (Lebowitz, 2000).

Within Chinese economic debates, Kornai’s influence has towered above that of any other contemporary foreign economist. In the 1980s his analysis of the relationship between shortage, investment hunger, and soft budget constraints was keenly studied by Chinese economists and senior leaders (Gewirtz, 2017).

Looking back to the break-up of the communist system in Eastern Europe, the political scientist and Sinologist David Shambaugh argued that there was a complete lack of foresight within Western academic and policy-making circles about the impending 1989 collapse of Eastern European and Soviet socialism. He observes that among recognized Western analysts, only one person, Zbigniew Brzezinski, had predicted the collapse of the USSR and the socialist system in advance (Shambaugh, 2008, p. 12).

When Kornai’s *Socialist System* was first published in 1992, the drama of the fall of the Berlin Wall and the collapse of the socialist bloc overshadowed his sophisticated and comprehensive investigation into the causes of its failure. It was hence largely ignored (Chirot, 1993, p. 855).

After 1989, China’s system did not collapse. Despite its development into a world power, Kornai believes that ‘China is not an “exception” that

refutes (his) theory' of systemic transformation, rather; 'It can be fitted, without difficulty, into the analytical scheme outlined [...] Furthermore, a still bolder statement can be risked: the analytical scheme provides a useful tool for analyzing the Chinese transformation in depth.' (Kornai, 2008, p. 150)

This thesis challenges Kornai's assessment of China by first dissecting, and then applying his theory to an analysis of China's political economy. In the first chapter, I present the key aspects of Kornai's 'socialist system' with the main focus on 'reform socialism'. In chapter 3 I compare Kornai's reform socialist model to contemporary China.

2.2. The system's paradigm

János Kornai's study, *The Socialist System, The Political Economy of Communism* (Kornai, 2007 [1992]), offers a valuable method to understand socialism¹ by abstracting systemic characteristics and using them as tools of analysis. Kornai locates his 'systems paradigm' as a methodology representing an intellectual tradition begun by Karl Marx, who viewed capitalism's political, economic, social and ideological spheres, '*altogether and analysed interactions between them... looking at the sum of its institutions –not one part or the other, but at the system as a whole.*' (Kornai, 2008, p. 186) Those thinkers who '*share the common conviction that a comparison of capitalism and socialism is worth analysis as research*' are also included in Kornai's systems paradigm tradition (Kornai, 2008, p. 187).

The system's paradigm seeks to study:

- The system as a whole and the relations to its parts
- Societal interactions by combining social scientific disciplines
- Institutions within which transformative societal processes occur and the identification of their system specific or non-systemic genesis
- Human organisation in the light of historical processes
- Systemic impacts on individual preferences

- Great transformations and big changes, uncovering underlying processes of decay and creation that lead to systemic transformations
- The intrinsic dysfunctional features of a system

Systemic attributes by comparative analysis (Kornai, 2008, pp. 190–193)

This chapter is a study of the central theses and main features of Kornai's analysis. It is designed to help identify commonalities and differences between Kornai's theory of socialism and 'socialism with Chinese characteristics', the self-definition used by the Chinese Communist Party to characterize its social system.

Kornai acknowledges that Marx only offered a minimalist definition of socialism and spent most of his time studying the capitalist system - predicting that it would be superseded by socialism. However, for Marx, only the advanced capitalist countries could provide the material foundation for socialism.

2.3. Kornai's theory of causality

Kornai's socialist system refers exclusively to those countries governed by Communist Parties. The system's 'genetic code' automatically generates 'classical socialism' when the Communist Party holds state power. And it shapes the features and fundamental characteristics of the system through three main lines of causation.

The first line of causation stems from the *rule of a Communist Party* guided by the ideology of 'Marxism-Leninism'; the second, from the *dominance of public ownership* within the economy; the third, from the preponderance of *bureaucratic coordination*.

The political system and ideology bring about the dominance of public ownership by design, and the combination of these first two lines of causation inevitably produces '*the dominance of the mechanism of bureaucratic control*' (Kornai, 2007, p. 363). Once the system of

Communist Party rule is established, it finds real roots in society and does so with only limited resistance. The system is internally coherent and self-sustaining (Kornai, 2007, p. 369).

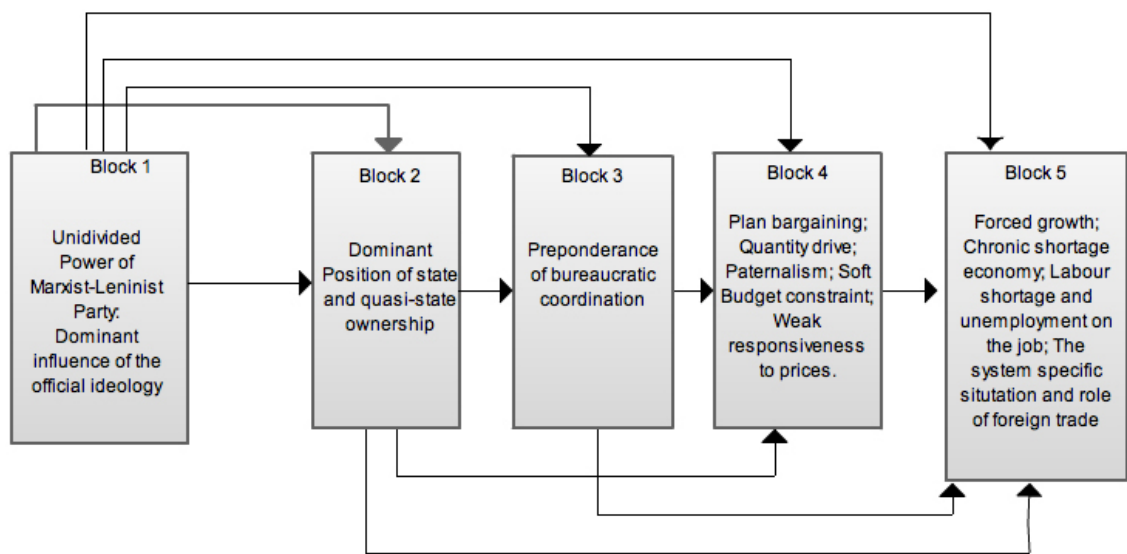


Figure 1. Kornai's main lines of causation under socialism

(Kornai, 2007, p. 361)

From three primary lines of causation (blocks 1, 2 & 3 above), subordinate features flow naturally and organically. The content of subordinate blocks (4+5) can vary significantly.

All countries where the Communist Party led an indigenous revolution were characterized by backwardness and poverty. The pre-revolutionary order was brutal, and democracy and capitalism were immature. These factors helped to shape and define the characteristics of the post-revolutionary regime. It was envisaged that backwardness would be overcome by forced growth, radical redistributive policies would be enforced by dictatorial measures; features Kornai describes as common to all socialist societies (Kornai, 2007, p. 373).

Kornai's analysis of socialism draws on Karl Marx's method for inspiration. It emphasizes the examination of social relations between people - between superiors and subordinates - those who exercise power and those who obey them. Kornai studies the complex relations between

economics and politics, depicts the social features that shape the values adopted, and the choices made by decision makers (Kornai, 2007, p. 12). He examines the historical realities of those systems that claimed to be socialist and identifies regularities i.e., patterns of recognisable human behaviour within a historically specific socio-economic system.

The 'classical socialist system' that Kornai dissects, first emerged in the Soviet Union under the leadership of Joseph Stalin. It was reinforced by measures such as the state requisition of peasant produce after 1928. In turn, this provoked widespread sabotage of agricultural production by the peasantry. Stalin responded to this with the forced collectivisation of agriculture.

In order to identify the main regularities of the socialist system Kornai examines these societies before socialist revolutions occurred. His focus is on revolutions where indigenous communist forces played the central role in taking power.² These countries shared basic features:

- They were poor and backward countries with low per capita production compared to advanced capitalism
- The agrarian economy was dominant with weak industrial development
- Modern and technically advanced sectors were very limited
- Pre-capitalist social relations and property forms still existed
- There were grotesque levels of income inequality
- They were dictatorial regimes using political repression
- Many of these nations were dominated by wealthy or colonizing countries
- They suffered from institutional instability caused by military conflicts of some form

In East European countries occupied by the Soviet Union in 1945, socialist systems were established by 1949, after a brief interregnum in which a mixed economy existed alongside a multiparty democracy. The Red Army destroyed the pre-1945 system of power. The apparatus of

Soviet administrative power exercised ultimate control and helped to forge a new state apparatus led by pliant pro-Soviet local communist parties (Kornai, 2007, p. 30). East Germany and Czechoslovakia were the only developed industrial countries, which underwent the transformation to a socialist system. But 'these countries were, so to say, compelled by open and concealed Soviet intervention to adopt a system whose first historical realisation had developed in a backward society.' (Kornai, 2007, p. 26)

Kornai regards the example of the Soviet Union as the 'purest' form of transformation into a socialist system. Indeed, it was also a popular, mass, urban revolution - more in line with Karl Marx's own concept of a revolution led by the working class. The transformation to socialism through the revolutionary overthrow of the old order was, as Kornai explains, circumscribed by backwardness. Indeed, in his view, it is the backwardness of the economy that 'induces revolution and allows the Communist party to seize power' (Kornai, 2007, p. 28). In order to establish the material foundations for socialism, the Soviet revolution needed to increase output and the productivity of labour and improve the living standards of the mass of workers and farmers.

After the Soviet revolution, as Kornai explains, a *revolutionary transitional era* began. This was a 'heroic' period, characterized by popular engagement and participation. It corresponds with the process of radical expropriation of the land, property and productive resources of the private economy. Where food resources are scarce, rationing and price controls are imposed to guarantee access for the poor. And popular policies to provide mass education and health provision are introduced. In addition, historical injustices produce spontaneous and state-led movements to persecute representatives of the old order. The consequence was an escalation of violence and lawlessness (Kornai, 2007, pp. 19–30).

Kornai notes that eventually, the revolutionary cause loses some of its lustre. The people begin to concentrate on their own material needs.

Production to satisfy material wants inevitably begins to take priority. The sense of encirclement by hostile forces creates an urgency to grow the economy rapidly. To achieve this objective, a disciplinary hierarchy is created. Bureaucratic procedures and methods of rule crystallize and generate institutions that are also organized along these lines (Kornai, 2007, pp. 26–29). Kornai rejects all theories that suggest that the system was never really socialist. He focuses instead on how the existing system operates by identifying its common features, contradictions and regularities. Two main systemic prototypes become consolidated after an initial revolutionary transitional period: classical and reform socialism.

2.4. A summary of Kornai's three main lines of causation under socialism

The following pages summarize the three main lines of causation that operate in both of classical and reform socialism.

2.4.1. The Communist party rule and ideology

The ruling Communist Party presides over a one party state. Where other parties are permitted, they are completely subordinate to the Communist Party. The party is a voluntary body, whose branches are headed by a party secretary. They function under territorially divided hierarchies. At the pinnacle are the Central Committee, its Politburo, and the General Secretary. Under 'democratic centralism' leading bodies are elected and can pass resolutions. Debates are held inside the party and voted on, and decisions are binding on lower organisations and individuals. All members must act on decisions without dissent. The party apparatus is composed of elected officials and unelected appointees, whose power emanates from bureaucratic authority. The upper levels of the party select and groom future members of the party apparatus. The party apparatus makes decisions about membership, promotion, demotion, or expulsion. The state and the party are organically intertwined as all candidates in elections to government are selected or vetted by the party. Government organisations are shadowed by parallel party organisations

that monitor operations and ensure that party instructions are implemented. Political and administrative functions are unified in the 'party-state' (Kornai, 2007, pp. 36–39).

Mass organisations of the youth, trade unions, women, minorities, artists, etc. also exist but they are subordinate to the party leadership and adhere to party decisions. The totality of the organisational power of the party and functionaries in the state, mass organisations and economy, constitutes a collective *apparatus* or *bureaucracy* (Kornai, 2007, pp. 39–40).

The bureaucracy is bound together by four main factors:

1. Marxist-Leninist ideology and a sense of serving the people and mankind.
2. The collective power to rule over society and the power to rule over subordinates.
3. Prestige and privilege: the former is derived primarily from rank in the bureaucratic hierarchy, the latter from access to goods and services in limited supply or of superior quality.
4. Coercion: decisions of the party and state must be implemented and defended, and are backed by sanctions, discipline or punishment in the event of either failure in practice, or perceived ideological deviation (Kornai, 2007, pp. 40–43).

The state is totalitarian in three senses; firstly, it extends to every aspect of life and there is no clearly defined private sphere; secondly, it reaches the whole society, and, through creating and monitoring comprehensive individual files, influences every citizen; and finally, decision-making and the legal system are subordinate to the particular and contemporary interests of the bureaucracy (Kornai, 2007, p. 48). Sectional, regional, industrial, organisational, ethnic, generational and other interest groups, inevitably emerge to constitute informal pressure groups - particularly when controversial issues are discussed and debated and when extreme repression is relaxed (Kornai, 2007, pp. 44–45).

Under reform socialism the monopoly of Communist party power continues in three key areas.

1. Party appointments remain ubiquitous in the state, economic management, the judiciary, and mass organisations. The public elect candidates nominated or approved by the party and bureaucratic apparatus. Limited competitive elections may be permitted, some are sham, others, are real conflicts between individuals, ideas and programs. Individual political representatives may conflict with official views and policies and this sews the seeds of a multiparty system (János Kornai, 2007, pp. 410–411).
2. Government continues to be exercised by decree. There is no separation of legislative, executive and judicial power, and thus appeals against organs of the state are excluded. The Communists have a solid majority and decisions are based on decrees rather than parliamentary procedure. In the reform era, demand for the 'rule of law' is raised, in order to subject all to judicial control, but the law is adjusted to serve the bureaucracy and the party (Kornai, 2007, p. 411).
3. The organs of armed force and repression remain under control of the party. It decides appointments, promotion, demotion, budgets and material resources. Armed force remains in the hands of the party leadership and is not subject to any endorsement procedure within the legislature. The classical and reform socialist eras do not differ in this respect (Kornai, 2007, p. 411).

2.4.1.1. Ideology under classical socialism

The classical ideology itself is based on a combination of intellectual foundations: from Marx and the tradition of the European labour movement; from revolutionary movements in countries that became socialist; from the experiences of Communist parties shortly after seizing power; or from consolidated systems of power. National variation and the selective use of these ideological layers, form the basis from which the operative ideology is created. Socialism is held to be inherently superior to capitalism because planning is believed to be capable of harnessing innovation for the collective good by eliminating anarchic market

relations, associated fluctuations in supply and demand, and overproduction crises. It should reduce the competitive duplication of effort, place human labour at the centre of society, and eradicate parasitical class exploitation and attendant luxury consumption. It is also supposed to unleash workers' ingenuity and enthusiasm, reduce supervisory costs, and lay the basis for such a high level of productivity under communism, that wage labour and the monetary system itself disappears (Kornai, 2007, pp. 49–51).

Classical socialism promotes a sense of moral superiority and focuses on overcoming individualist and selfish 'remnants', and on creating a self-sacrificing and collectivist psychology that promotes social justice and egalitarianism. Ideologically convinced believers in socialism see its existence as the pathway to human emancipation, so they view specific failings, crises, or limitations in performance in this context. Open competition with alternative ideologies is forbidden, although religion is sometimes tolerated. Directly oppositional ideologies can only survive in underground publications or during short periods of openness. Kornai argues that a breakdown in belief in the inherent superiority of socialism is a characteristic of departure from the classical system (Kornai, 2007, pp. 52–53).

A gulf exists between economic development in advanced capitalism and socialism. The superiority of the latter system is supposed to provide the base from which to catch up with and overtake capitalism. This requires the general mobilisation of enthusiasm and resources to stimulate rapid growth and assure future victory. Welfare systems radically reduce inequality, unemployment is minimised and the state assumes a wide range of obligations in relation to basic needs and services. This ensures security in health, education, housing, employment, pensions, holidays and access to cultural facilities. Thus a tension emerges between the burdens of social provisions and the need for rapid economic advancement (Kornai, 2007, pp. 53–54).

Party rule is legitimized by its claim to be a vanguard party, incarnating the historical interests of the most advanced class, the proletariat, whose dictatorship is normally backed by an alliance with the peasantry. Opposing forces are represented as class enemies or misguided allies, who require education to overcome 'petty-bourgeois' prejudices. The vanguard party's ideology boasts of farsighted understanding of historical processes and societal needs. Ideological paternalism is combined with the ubiquitous provision of all basic needs. This paternalism may promote a cult of the individual and serves to justify centralism and bureaucracy (Kornai, 2007, pp. 55–57).

The moral imperative is characterized by discipline, loyalty, duty and submission to needs and objectives defined by the party and state. This can be traced to Communist practices in the pre-revolutionary underground struggle, which variously entailed, armed struggle, insurrection, and civil or guerrilla war; conflicts in which discipline and obedience are necessary and highly valued qualities. In the era of post-revolutionary transition, establishing the social order and reinvigorating economic activity, also required discipline and sacrifice. Those who serve the cause are regarded as heroes and revolutionaries, and those who don't, are observed and graded in relation to their utility or hostility toward the system. The hostility of anti-communist forces, externally and internally, fosters and reinforces a siege mentality (Kornai, 2007, pp. 57–59).

The maintenance of power is an ideological objective in itself and how firmly this power is held is a decisive criterion of success. Power and ideology are inextricably interconnected. Ideologically motivated people shape the organs of the party and state. The need to legitimize and justify the actual system results in adjustments and modifications to the ideology. The classical system '*develops and consolidates only where this official ideology of socialism just described enjoys a commanding influence*' (Kornai, 2007, p. 61).

2.4.1.2. Ideology under reform socialism

Multiple contradictions and pressures inevitably find expression and force revisions to the party's ideology, but party ideologists seek to minimize adjustments to safeguard fundamentals and to justify the present line.

However, under reform socialism certain tenets remain untouchable:

- a. The leading role of the party in the state, the ban on factions and adherence to democratic centralism inside the party.
- b. The doctrines of Marx and Lenin are untouchable; errors are blamed on their misinterpretation.
- c. The superiority of public ownership and its predominance as the foundation of socialism.

Where it was previously taboo not to declare allegiance to these untouchable principles, now it is self-censorship that prevents the explicit questioning of them. Underground literature and groups engage in dissent against the core axioms. If this dissidence on the fundamental taboos becomes a widespread, vocal and mass phenomenon, it may signal a change from reform to revolution.

Ideological flexibility leads to creative pragmatism but weakens the bonds between the people in command of society. Certainty of mission and the sense of superiority over capitalism are undermined. Material incentives come to replace ideology as key motivators but during economic hardship, appeals to moderation may reappear. A retrenchment of the state from comprehensive welfare provision, subsidies, and other social guarantees, is accompanied by an emphasis on personal responsibility. Taboos gradually break down, and a weakening of ideological cohesion is reflected in the media and education. The press, radio and television become a terrain where the pressures of social opinion find critical expression (Kornai, 2007, pp. 414–418).

2.4.2. The dominance of public ownership

Classical socialism is characterized by a massive preponderance of public ownership as a percentage of national income. The property rights of state-owned firms and other publicly and semi-publicly owned entities are inalienable. Bureaucratic administrators hold no property rights, and their incomes are not determined by the profits of these state companies. *'State property belongs to all and to none'*. Nevertheless, the bureaucracy exercises *'some of the rights of ownership and all of those of control'* (Kornai, 2007, p. 75). There is no profit motive determining the actions of socialist firms in the classical system. Private sector activity is almost totally eliminated. It is regarded as a hostile force and it is largely confined to informal and illegal 'black market' activities. During classical socialism state-owned firms occupy the 'commanding heights' allowing non-state sectors to be dominated. The residual income is difficult to identify and is broader than the quantity of taxes and profits. The bureaucracy determines all operating conditions, and all income and expenditure is part of the central state budget. However, individual bureaucrats are limited in their disposal rights by various rules and regulations (Kornai, 2007, pp. 71–73).

2.4.3. The dominance of bureaucratic planning

The bureaucracy exercises control rights over state-owned production through a pyramid of power dominated by vertical hierarchical control. Overlapping bureaucratic organisations regulate and control individuals and organisations. They include, the political police, the youth organisation, the trade unions, the women's organisation, the work unit, etc. All organisations are subordinate to the party structures and hierarchy, which have their own supervisory and disciplinary apparatus. State administration and governance is supervised legally and administratively and by mass organisations, and the population is also administered where they live. The ubiquitous nature of supervisory systems in the classical system, in theory, allows for failures to be

spotted and rectified by multiple organisations. Commands downwards to subordinates can be issued, and subaltern groups or individuals can express disagreement, provided they do not challenge the fundamental tenets and principles of the system of power. The system provides no means to opt out or 'exit', as leaving any institution, moving home, changing job, leaving the union, or party, entails bureaucratic complications, possible sanctions, or worse (Kornai, 2007, pp. 97–100).

In the classical system planning is comprehensive; it encompasses production targets for the main economic sectors; the use of their products; a rationing mechanism for distribution, and quota systems for inputs. Balance between the sources and uses of production are agreed between relevant parties, and equilibrium is sought. Planning encompasses labour quotas, wage levels, investment, high priority projects, technical development, foreign trade, trade relations, and the balance of import-export ratios. It also includes finance of the state budget, banking and pricing.

Plans are subdivided between planning bodies, ministries and enterprises. They are imposed on lower level organisations, but some scope for amendment is negotiated in advance of the final plan. Fulfilment reports are required after implementation (Kornai, 2007, pp. 111–114).

In the classical system the bureaucracy decides on the formation, liquidation, break-up or merger of firms and determines appointments, promotions, the dismissal of leaders, and the parameters of managerial decision-making within the plan. Products and materials are allocated in such a way that *'the bureaucracy takes the place of the market mechanism'* (Kornai, 2007, p. 116). Upper levels of the hierarchy exercise direct bureaucratic control by constantly intervening in the operation of subordinate bureaucratic entities. Despite its rigidity, the absence of market impulses, and limits on innovation, *'the tasks those running the system consider of primary importance are particularly likely to be accomplished.'* (Kornai, 2007, p. 117)

Bureaucratic motivation is distinct from proprietary motivation, as no residual income benefits are derived from innovative decision-making. Supervision and sanctions from above tend towards a conservative passivity shaped by bureaucratic dependence. Individual bureaucratic motivations may be driven by ideological conviction, professional satisfaction, power and prestige, material benefits, the desire for a quiet life, and the fear of sanctions from above (Kornai, 2007, p. 119).

A form of vertical bargaining emerges between bureaucratic entities. The lower levels seek a simple means of fulfilling their tasks, so they request excess labour and supplies. The higher level seeks to extract more production, so prescribes tighter plans than are realistic, in expectation of the impending bargaining process. This process pertains between each superior-subordinate relation of bureaucratic power (Kornai, 2007, pp. 122–124).

Bureaucrats are not concerned with present and future profits, corporate value, market position, or commercial concerns. The top leaders pursue a drive for rapid growth. Attempts by lower level bureaucrats to match these demands are tempered by conflicting concerns with quality, and by bargaining interests, which seek to minimize change. Planning in the classical system is inextricably interconnected with politics: as managerial, technical, bureaucratic, and political roles, are the combined and complementary faces of the bureaucracy when it negotiates about resource allocation, tasks, etc. (Kornai, 2007, pp. 124–127).

The interests of those who provide planning information, the quantity of information required and the rigidity of the implementation system all compromise its quality. Adjustments to the plan inevitably have unexpected consequences. Thus a hierarchy of priority plans is devised, which result in the relegation of plans of subordinate importance (Kornai, 2007, pp. 127–130).

2.4.3.1. Forced growth: an automatic dynamic of the system

The objective of Communist Party leaders in developing countries is to escape from backwardness, and become developed countries. Socialist economic management is believed to be in a superior position than comparable capitalist countries, as the mobilization of resources and manpower is freed from the dominance of imperialist control, and the limitations of profit-seeking companies. The speed of growth is considered to be the decisive indicator of progress. Kornai's analysis of socialist investment and growth patterns looks at long-term trends and the motives of the protagonists shaping the institutional framework and dynamics. It examines what determines the rate of growth and the motives of the leaders.

Plans are imposed from above to achieve optimal growth. The drive to pursue rapid growth is replicated amongst middle and lower level leaders who also have "a strong inner expansion drive" and support the same ideological objectives. The expansion drive corresponds to their bureaucratic motivations and objectives. When an institution expands, the prestige and power of its cadres is enhanced. In hospitals, schools, universities etc., there is always pressure to satisfy unmet demands. This also applies to the products and services of state owned enterprises. In capitalist enterprises the potential gains from expansion are tempered by the risks of expansion e.g., concerns about competitiveness, market size, prices and profits. Within classical socialism, shortages and a lack of competition mean that increased output inevitably finds a buyer. And soft-budget constraints mean there is no financial discipline imposed. So, without private ownership there is no incentive to curb "investment hunger". Although Keynesianism encourages state investment under capitalism, it does so to encourage the "animal spirits" of private owners. Under socialism, however, the only limit to investment hunger is the bureaucratic fear of sanctions for making 'wrong decisions' (Kornai, 2007, pp. 160–163).

Before investments are made, a top-down distribution of funds is

organized through the national plan, which is generally divided between basic needs and priorities for development. The plan is not simply a one-way command; it is the product of a bargaining process. Lower-level entities demand more than higher-level entities wish to offer and investment priorities outnumber the resources to match them. Negotiations between superiors and subordinates stretch the plans towards over ambitious targets. This may involve deliberately underestimating costs to get in on the plan. Profits do not determine if a project is deemed viable. Investment is concentrated on priority projects. The planning process involves the identification of shortages and the means to overcome them, and the elaboration of new spheres of production. Excess demand for investment goods and services stretches available resources, and higher-level organizations are forced to intervene to determine allocation priorities. Those projects lacking resources must delay completion, which increases costs. Nevertheless the projects continue, as they represent bureaucratic lobbies. This system is inflexible and unresponsive to unplanned circumstances and opportunities (Kornai, 2007, pp. 163–165).

A fetish for large-scale investment projects, which consume vast resources and assume a gigantesque scale, compliments the focus on rapid growth. In addition the concentration of power over investment decisions is the responsibility of a small number of people. Under capitalism, investment and spending decisions are decentralized and individualized, whereas in classical socialism an extremely centralized structure of decision-making, shapes investment and spending through the restriction of consumption. The proportionate relationship between the growth of investment and consumption is shaped indirectly; to the degree that leaders sense popular discontent and adjust policies to contain this. Concern for the welfare of the masses is expressed in multiple documents from the leadership but the focus is defined by political expediency. Nevertheless, throughout long historical periods consumption may rise, although, from 1949-1978 consumption stagnated in China. A thirst for investment in resources is engrained in the micro and macro level motivations of the bureaucracy at all levels of power.

Their motivations coincide with each other. Therefore, the central leadership's drive for growth expresses the will of the entire bureaucracy.

A mutual interrelationship exists between the power structure, ideology and property relations, and the character of investment and growth. The maximization of growth over 10 or 20 years is prioritized over present consumption. Sacrifice for the future is a central demand but public tolerance is limited e.g. if it entails inadequate food rations. The postponement of consumption involves a growing under-utilization of resources, buildings, stores, consumer goods factories etc. and such neglected investments may have long-term detrimental impacts on society, for example on the environment and in health care (Kornai, 2007, pp. 165–170).

The production of fixed capital investment goods assumes the leading role. This generates a cycle of reproduction, which produces even more fixed capital investment. *'There is sense, therefore, in speaking of an internal spiral (or propeller), because the spiral motion advances, resulting in evermore investment, evermore fixed capital, and ultimately, ever more aggregate output.'* (Kornai, 2007, p. 171)

This driving force pulls other sectors around it like a magnet and so decision-makers tend to structure planning procedures and priorities in ways that replicate the original design. The subordinate priorities adopt a similar pattern of investment. Domestic production is elevated over imports, in line with autarkic development planning. The Marxist distinction between productive and unproductive labour is interpreted as one between tangible material products and 'intangible' services. The lack of democratic control leaves decisions in the hands of bureaucrats rather than consumers. Such bureaucratic priorities are insensitive to the vicissitudes and complexity of consumer demand. Therefore, the postponement or neglect of service provision is commonplace.

The production of the means of production takes priority over consumer goods production. Heavy industry is seen as the most rapid path to

mechanization and technical advance. Top priority projects are assisted by a highly centralized system that concentrates resources on primary objectives. These sectors grow extremely rapidly while consumer goods production, housing, communal services, trade, agriculture and transportation all tend to lag behind (Kornai, 2007, p. 173).

The importance of the arms industry intertwines it with the internal spiral driving the economic system. At the micro level these driving forces and priorities focus on new installations that represent spectacular advance, progress, and modernity. This is simultaneously designed to stimulate workers enthusiasm and to boost production. However, the neglect of older factories, housing stock, universities etc., is the other side of the coin.

Gigantic mega-projects are like bureaucratic fiefdoms, which take centre stage in national planning. They are justified on the basis of economies of scale but this simultaneously ignores the notion of an optimal scale, which should be defined by technology, skills, market structure, administrative competence etc. These factors may augur against single giant entities from the standpoint of rationality, responsiveness to demand, and quality control. However, fewer subordinate entities are easier for upper-level bureaucrats to control.

So, for example, where the steel industry is given top priority, agricultural machinery made of steel may also become a priority sector. However, the multiplicity of components, infrastructure, repair services, storage facilities, etc. lags behind, and this causes a dislocation in the proportionate relations of such economic 'ecosystems'. This leads to breakdowns in the production process and shortages. Planning by such methods inevitably produces an information deficit in the regulation of complex interrelationships and dependencies - a role that prices play in a capitalist economy.

A priority investment project promoted by the leadership, when first authorized, will generate an indecent haste, rush, and forced growth. The

achievement of priority plans by definition involves the neglect of other, perhaps equally important projects. Neglect also takes the form of environmental impacts such as the degradation of soil, air pollution, water pollution, etc. Little is done to ameliorate the negative consequences of this investment priority structure. It is perfectly true that capitalism is also destructive to the environment, as profit seeking has no inherent bias to environmental protection. However, bureaucratically driven forced growth, combined with a lack of democratic means of expression, excludes supervisory mechanisms that might act to check excess and neglect.

Forced growth has as its objective the maximization of aggregate output and improvements in corresponding statistics. These objectives are limited to the medium-term of 10 to 20 years. Consequently, **these priorities organize the structure of the economy**, which becomes fixed in a disharmonious state (Kornai, 2007, pp. 174–180).

An examination of extensive and intensive methods of growth allows us to differentiate between capitalist and socialist methods. The factor output relationships can be divided into two groups. The first concerns the impact of growth of the capital or labour expended on production, which causes a proportionate growth in output. The second concern is raising productivity through the effective exploitation of capital or labour. Kornai explains that the term ‘extensive growth’ has the same meaning as ‘factor growth’ used in capitalist economics; and the term ‘intensive growth’ refers to ‘factor productivity growth’ (Kornai, 2007, p. 181).

The use of extensive methods of growth stems from the original state of backwardness and the poor exploitation of resources. The potential to increase the labour force is revealed by unemployment, underemployment, and the low level of female employment. The number employed grows rapidly as capital and labour is brought into play. A high investment ratio is combined with rapid employment growth. The lack of fixed capital means that lengthening the working day or increasing the number of shifts worked on the same plant can maximize its exploitation.

And a lack of worker representation limits resistance to this. However, as the reserves of labour are used up this strengthens the hand of the labourer. Farmland is also extended to the maximum degree possible and natural resources are treated in a similar fashion. The economy resembles an economy mobilized for war.

Intensive methods are combined with forced growth. In theory, socialism is supposed to unleash latent energy and enthusiasm on the part of the workers. However, after an initial boost, as time passes a more apathetic mood sets in, which is exacerbated by everyday problems such as the lack of consumer goods. Technical advances introduce new technologies and science to backward areas, although this often takes the form of replicating and imitating production that already exists in capitalist countries. The concentration of investment and rapid growth requires skilled labour, but the development of these skills lags behind.

Bottlenecks and stoppages cause disruption to production. The quality of goods is hindered by the lack of resources and the urge for speedy production. The capitalist desire, to innovate production technique to gain a first entrant advantage, is completely lacking. Instead there is a bias towards achieving growth rates and targets based on the quantity of production. The use of services at their optimal level is confused with over intensive use: such as packing people into trains or buses, the inadequate provision of housing, and overcrowding in educational institutions.

The application of intensive methods known as total factor productivity plays a minor role in socialist economic systems and plays a far larger role in capitalist economies (Kornai, 2007, p. 186).

2.4.3.2. Socialist economic cycles

The economic cycles under socialism are distinct to those under capitalism. The economy fluctuates with the planning calendar. During annual plans, the pace of work increases as the plan period comes to an end; and, as the new planning year begins, work slows down. However,

a new Five-Year Plan produces a less pronounced fluctuation, and it usually signals the start of many new investment projects.

Some countries experienced more dramatic shifts from rapid growth to decline than others. The central system-specific cycles resemble stop-go phases. These are characterized by sudden changes, slowdowns and stagnation; which is followed by slow and then rapid expansion, and again slowdown and stagnation.

Expansion and contraction are characteristic features of capitalist cycles but are caused by different factors. Capitalist cycles often take the appearance of crises of demand - overproduction - in which profitable investment opportunities are lacking. However, investment decisions that lead to a slowdown are spread horizontally through the independent and decentralized decisions of company owners. In socialist economies the brakes are applied by central control, and instructions to enforce this are carried out by command from above.

Neither the falling rate of profit, nor inadequate demand, is the causal factor of economic crises. Rather, braking mechanisms are applied because the resources to drive accelerated growth are lacking.

'The entire cycle takes place amid conditions of rush, expansion drive, investment hunger, investment tension, and chronic shortage. These mark the conduct of decision-makers at all levels in the bureaucracy. They would like to invest as much and as fast as possible; meanwhile they meet constraints at the peak of the cycle that rule out further acceleration. One might put it like this: the top leaders receive signals notifying them of the obstacles to further acceleration.' (Kornai, 2007, p. 191)

The signals that provoke a slowdown may be debt or import dependency; investment tensions that cause ever more common interruptions in the process of production and distribution; or discontent amongst the masses at restrictions on consumption caused by expanded investment. These

factors may occur individually or simultaneously. And with such a system, whose mechanisms of administration are on a particular path, this inevitably means that responsiveness operates with a time lag. Therefore slowdowns and periods of acceleration are themselves punctuated by several phases. Adjustments through the period of slowdown permit the bureaucracy to reassemble its forces and readopt its default mode of operation - forced growth. In addition, changes in political leadership can provoke dramatic shifts in policy. It is certainly true that socialist planning failed to produce smoother growth - free of fluctuations - as envisaged by those who originally sought to overthrow capitalism (Kornai, 2007, pp. 190–193).

Distortions of data are commonplace as socialist countries used different accounting methods; and the productive sphere was valued more highly than the service sector. In addition, because prices were not fully responsive to supply and demand they do not reflect quality and emphasize quantity. The main features of growth within a classical system of socialism differ to those under capitalism and to those in the developing capitalist countries. The key feature of growth under socialism is the acceleration of tempo forced from above by the bureaucracy. This leads the economy 'to run faster than its legs can carry it' (Kornai, 2007, p. 197). Typical forms include: high investment and low consumption; priorities determining investment; accelerated exploitation of extensive development; and quantity over quality.

However, none of these features constitute a strategy intentionally pursued by the leadership: 'no one adopts a conscious policy of neglecting quality, overstretching utilization of the service sphere, damaging the natural environment, in some periods reducing consumption, and so on. Yet the combination of the main features forms an organic whole: the planned and spontaneous priorities, conscious and instinctive methods, and desired and undesired consequences go together. After all, these features were not chosen according to a particular planner's own preferences. This type of growth and the accompanying behaviour and mutual relations of those taking part are

formed largely by their social situation, which circumscribes the scope for decision-making. A combination of prevalent power structure, ideology, property relations, and coordination mechanisms, together with the systems initial state characterized by poverty and backwardness, sets the process of growth on the system specific path described' (Kornai, 2007, p. 198).

Despite Kornai's normative rejection of socialism he recognizes that 'classical socialism certainly took many countries from a state of severe backwardness at least to a medium level of development.' (Kornai, 2007, p. 202)

2.5. Kornai's definition of reform and revolution

Kornai argues that the classical socialist system constitutes a coherent entity. Its breakdown and demise is driven by impulses that come internal contradictions and dysfunctions. Economic slowdown exposes shortage and waste and the technical lag compared to advanced capitalism. Forced growth leads to neglect in spheres such as health, housing, transport and telecommunications, and military budgets restrict consumption. Public disaffection with consumer goods, the natural and built environment and low living standards, grows. Bureaucratic power and propaganda clashes with a desire for greater freedom of expression and action, particularly amongst the intelligentsia. Unity amongst the elite dissipates as self-doubt replaces self-confidence. The international experience of reforms and revolts in other socialist states, impact all such states. This was evident in 1989 where, regardless of repression or control over propaganda, even isolated states experienced common upheavals (Kornai, 2007, pp. 383–386).

Kornai provides his own contextualized definition of 'revolution' and 'reform', in which, any change that fails to radically amend the three core lines of systemic causation (party rule, public ownership and bureaucratic coordination) cannot be considered as reform. Changes restricted to subordinate spheres are defined as '*superficial phenomena in economic*

activity' (Kornai, 2007, p. 388), and are not classified as reform. Reform must impact one of the three main lines of causation and affect the functioning of this sphere fundamentally and permanently, and yet not so fundamentally as to change the system away from the socialist 'species'.

'Revolution' as defined by Kornai means ending the undivided rule of the Communist Party as the precondition for a qualitative change of system. He rejects the view that revolution is defined by rapidity, origin 'from below', or violence. The term revolution is defined as a qualitative leap from one family of systems to another, not by whether it is considered to be an advance or a retreat. *'A consistently radical change in the deepest fundamental attributes of some society - that and only that is what in this book qualifies as a revolution.'* (Kornai, 2007, p. 390)

When long-term ailments find expression, the trigger events are diverse. It might be the death of a leader (Mao Zedong, Stalin), change from above (Tito), or initiatives from within the elite. Pressure from below may take the form of rumbling discontent or open revolt. The aim of Kornai's analysis is to provide 'abstraction distilled from the multiplicity of historical realizations' (Kornai, 2007, p. 394).

2.5.1. The perfection of control

Advocates of 'perfection' are supporters of the system, who seek to refine and perfect it. To eliminate problems within the bureaucracy they amend the instruments of power and control. Firms are merged for economy of scale, although comparative capitalist enterprises are generally smaller. For, under socialism, systems are designed for ease of control and monitoring. Thus monopolies without overlapping boundaries are efficient from the standpoint of bureaucratic simplicity.

Mathematical and computer models are employed to promote rational planning and control. But, as planning functions through 'vertical bargaining and horizontal reconciliation' (Kornai, 2007, p. 404), the concealment of information is in the interest of many officials. So, they

are hostile to computerized models that might expose this. However, Kornai maintains that the complexity of the calculations required to regulate a national economy are too intricate and uncertain to be calculable (Kornai, 2007, p. 405).

Plan indicators may be adjusted by decentralisation; amending their quantity and quality; focusing on net production or profits; and decoupling performance assessments that relate to past results (Kornai, 2007, pp. 405–406). Indeed, even elevating the profit motive to the chief indicator is, in Kornai's eyes, antithetical to capitalism if real decentralisation, free entry and free competition is missing (Kornai, 2007, p. 406).

After such experiments a new cycle of recentralisation re-emerges to restrict non-compliance, and to tighten up on dodges and tricks. More regulation, control, administrative layers and disciplinary measures are imposed. In this way, the 'perfection' tendency may serve to strengthen conservative tendencies. However, where political loosening accompanies these changes, it may help to 'break down the self-congratulatory official ideology'. A constituency, encompassing sections of the leading circles, comes to believe in more profound and radical change (Kornai, 2007, p. 407).

2.5.2. Market socialism

The principal concept behind market socialist ideas is for the market to fulfil the role of the basic coordination mechanism of the economy, or at least be equal in importance to bureaucratic planning, and for this to function in an economy dominated by public ownership. Various tendencies exist within this stream with differing ideas concerning how much power the market should have within the economy (Kornai, 2007, p. 474).

This constitutes one of the main trends away from the classical system. Kornai argues, that the idea of market coordination is alien to Marxist traditional theory, which sees the market as an anarchical system of

coordination. Marx proposed that market relations, reacting to supply and demand, would be replaced by conscious planning. Kornai believes that adopting market socialist ideas entails abandoning the axiomatic principles of Marxism (Kornai, 2007, p. 475).

For reform socialists, combining a 'plan-cum-market' appeared to offer the prospect of correcting market failure in the social sphere, and minimising the need for intervention by central planners in everyday economic operations. The system retains key features of the classical system and combines these, with independent firms, contractual relations, price signal tools, and other market based measures. Market socialist ideas emerged organically. Many thinkers in different countries independently developed similar ideas to one another. These theories play a central role in the new ideological line developed under reform socialism, in which the market is allotted a respected role in economic activity (Kornai, 2007, pp. 477–479).

Various 'socialist-market' methods were used over time. They involve a degree of 'deregulation' i.e. they remove economic entities from direct bureaucratic command (Kornai, 2007, p. 480).

There are differing criteria for assessing such deregulation.

- a. The degree: to which it impacts on central command.
- b. The scope: local, national, experimental, gradual, competitive, universal.
- c. The sequencing: sudden abolition of commands or gradual evolution.

The package of deregulatory measures differed substantially from country to country and experiment to experiment (Kornai, 2007, p. 481).

2.5.3 Self-management

Kornai identifies self-management as a political and ideological tendency that advocates economic democracy, workers' councils or soviets, as replacements for bureaucratic coordination. He describes this as a

socialist tendency. It can originate as a top-down national initiative - as it did in Yugoslavia from 1950 till the 1990s. But the *'idea of self-management recurs repeatedly in the debates on reform in other socialist countries as well'* (Kornai, 2007, p. 462).

This trend finds support in the ideas of Marx and Engels and envisages that workers' self-governance will replace bureaucratic coordination.

Kornai says:

'One leitmotif is strong condemnation of the role of the state and rejection of all kinds of 'etatism'. The ideal situation is a society with no state at all. What is needed is economic democracy and workers' self-organization.'

'Some elements of the ideas proclaimed by the intellectual current of self-management are realized in practice, at least in part. For instance, the historical formations like the Paris Commune in 1871, the soviets in the early days of the 1917 Russian Revolution or the short-lived workers' councils in the Hungarian Revolution of 1956 bear some resemblance to the intellectual model of self-management.' (Kornai, 2007, p. 462 [1992])

The concept of self-management that Kornai employs encompasses a wide range of phenomena. These include the revolutionary episodes just cited and a variety of trends that enhance the expression of workers' demands: from official trade unions becoming more militant; to the Yugoslav experience; where state and economic power was supposed to be an expression of workers' self-management. Yugoslavia is the most enduring example of this trend, where it was the guiding philosophy of the party and state for nearly 40 years (Kornai, 2007, pp. 461–473).

It is a trend produced by the political and ideological loosening of bureaucratic authority or even its disintegration. It is often promoted by Marxist believers but may also be supported by opponents of the system as a tactical measure to undermine the power of the party. Self-management may result in a loss of managerial authority, and a strengthening of the trade unions and workers' bargaining power. The

official state unions may start to display a greater degree of independence vis-à-vis management. In turn, managers will often adopt populist measures and represent workers' interests in negotiations with superiors (Kornai, 2007, p. 462 [1992]).

2.6. Hard and soft budget constraints

Kornai developed the concept of soft and hard budget constraints in 1980. These correspond to socialist and capitalist financing systems. Soft budget constraints pertain, when state firms under socialism consistently bargain with their superiors to increase their allotted funds without due regard for economic viability, profitability, etc. Soft-budgets can assume the form of bargaining for soft subsidies, soft tax bills, soft credit, and soft administrative pricing. Overall the soft-budget constraint expresses the collective experience of state owned entities in a socialist economy. Even if they make a loss, they are provided with funds and subsidies that ensure the enterprise remains in operation regardless of market conditions. A paternalistic relationship emerges between lower and upper level bureaucrats. The hard budget constraint assumes that profit maximization is the objective of the firm. If it is unable to make a profit, it is allowed to go bankrupt. Capitalist economic systems generally operate within hard budget constraints (Kornai, 2007, pp. 140–144).

2.6.1 Vertical dependence

Some key features of the semi-deregulation of state owned firms are cited here. There is dual-dependence upon vertical ties to state authorities and on horizontal ties to the market of buyers and sellers. The system specific features of these vertical dependencies are catalogued as follows:

1. Entry into the market to produce and sell goods is determined by bureaucratic decision and permission.

2. Exit from productive investment is also determined by bureaucratic decision, or halted by bureaucratically allocated resources producing a culture of soft-budget constraints for state companies.
3. Mergers and splits are permitted, but final rejection or permission is a bureaucratic right.
4. Appointment of leaders is decided or heavily influenced by bureaucratic powers.
5. Exports, imports and foreign exchange are less tightly controlled, but pressure is brought to bear to fulfil certain obligations or de-prioritise others. Technology or product development choices may be determined by superior organisations.
6. Prices are generally still subject to some control.
7. Wages are subject to pressures at the minimal and maximal scales, undermining free bargaining.
8. Taxes and subsidies are subject to considerable scope for tailor made solutions and the bending of rules.
9. Bureaucratic interests vertically control credit and loans; banks provide soft-budgets to save and sustain projects that are deemed important.
10. Investments are partially deregulated to firm level decision-makers, who can spend retained profits. In large projects, the state intervenes more frequently.

Free enterprise does not apply in the state sector and rivalry between firms is restricted. The survival or demise of state owned firms and managerial promotion or demotion within them, is determined bureaucratically. However, formal regulatory frameworks fail to account for a myriad of intangible means by which the leadership bend firms to their will. There is a far greater scope for evasion and personal decision-making, more fluidity in power relations and more bargaining between superiors and subordinates. Direct bureaucratic control of the classical system gives way to indirect bureaucratic control in the socialist-market (Kornai, 2007, pp. 482–489).

2.6.2. Budget constraints and the responsiveness of firms

Market-socialists hoped that reduced engagement in direct planning would free resources up to concentrate on short-term macro economic policy and long-term economic strategy. However, micro-regulation continues and old planning routines become useless. Kornai believes that socialist-market planning is not a strategy but rather 'a series of improvisations'(Kornai, 2007, p. 489).

The profit motive is supposed to incentivize the behaviour of firms. Investments are partially financed by retained profits in the hope that prices and costs will begin to shape managerial action. Budgetary laxity means that the correlation between profits, prices and actions, remains limited. Soft budgets take the form of subsidies, tax benefits, credits and administrative pricing. The maintenance and expansion of unprofitable firms, by rescues and bankruptcy avoidance, is financed by the state.

Vertical bargaining produces customized solutions. Rules are subject to incessant adjustment, subsidies and deductions are complex and unique, and relate to the specific spheres of interest of bureaucratic powers. High profit companies are squeezed to subsidize other sectors in a form of egalitarian profit distribution. Profits are conjured-up by bureaucratic action rather than being produced by market relations and incentives.

The Communist Party and the bureaucracy are not profit driven owners of firms, so, ideological conflicts occur between the paternalistic promotion of solidarity and workers' welfare, and demands to implement hard budget choices, particularly when this provokes workers' unrest.

Under capitalism, property ownership generates innate profit seeking motivations and behaviour. The market is governed by this universal discipline. Kornai believes that public ownership negates this, and cannot lead to the application of financial discipline, because ownership relations do not divide the bureaucracy. The state is the owner and manager rolled into one. This can only be changed by private ownership, or if state

enterprises are few in number and surrounded by capitalist enterprises (Kornai, 2007, pp. 493–495).

Entrepreneurial dynamism requires free entry into productive activity and access to credit for private individuals or companies. Market socialist coordination and control mechanisms involve micro-level decision-making on company activities by managers and their vertically superior bureaucratic organisations. 'The more bureaucratic control remains dominant, the less the budget constraint can be hardened' (Kornai, 2007, p. 495).

The root of this problem is seen in the power structure, property relations and coordination mechanisms. In an economy in which budgets are 'sufficiently weak to dampen substantially all demand and supply reactions, the market is incapable of fulfilling its role' (Kornai, 2007, p. 496).

These factors produce firms which react with dulled market responses to price signals, producing less effective and slower reactions than their private free-market cousins. Price signals from companies that are kept alive artificially, in turn produce more artificial prices.

The expectation of market-socialists was that firms would behave price-sensitively and financial control would replace physical input and output instructions. Investments would respond to interest rates and product substitution would be stimulated by prices. However, the firms were overwhelmingly unresponsive to these control mechanisms. Despite the more active role for money, public sector economics under market-socialism remains only semi-monetized (Kornai, 2007, p. 497).

2.7. The affinity between public ownership and bureaucratic coordination

Reformers hoped that market mechanisms would occupy the vacuum created by the control or dissolution of the instruction system, but

amended bureaucratic coordination filled the gap. Indirect vertical control predominates and is combined with subordinate horizontal relations.

The resistance by upper and lower level bureaucrats to implementing policy changes is often blamed for the situation. Kornai maintains that the bureaucracy is a 'hierarchically structured social group' rooted in every cell of society, so the natural survival instincts of this group pursue its continuance. They cling to their authority, identify with their respective organisational and social functions, and seek to complete them. They try to reinforce their rule and to perfect it. Firm managers want little interference from their superiors, but nevertheless seek out their superiors, and connections inside the bureaucracy, whenever difficulties are encountered. Their 'capital' is composed of these interrelations and these connections are their natural environment.

The attempt to match central control with independent firms is contradicted by vertical subordination. Bureaucratic self-reproduction is organically engrained in the system. 'There is no need for a central command; on the contrary, bureaucratic coordination rises again even if some stern central resolution lays down that it must be curtailed.' (Kornai, 2007, p. 499)

2.7.1 Horizontal relations of firms in public ownership

There is a substantial growth of horizontal relations in the reform era, but these relations are not governed by prices, profits or rivalry. Rather, they are the result of bureaucratic command. This market is a contrived affair, in which formulas and incentives are thought up and imposed, rather than naturally evolved. There is no affinity between the market and public ownership. Contracts are broken with impunity, companies refuse to pay, or pay late, leading to debt queuing by firms and general liquidity crises, and state rescue as a last resort is taken for granted. Company to company credit and debt is permitted, but so is delay, or the non-payment of debt.

Three forms of capital allocation for public firms emerge, central state budgetary funding, investment loans from state banks and investments from company savings. One method proposed, is to permit cross ownership is through joint - stock companies, which issue shares. Banks, insurance companies, pension funds and other state entities, hospitals, local governments and villages etc. are permitted to own and trade shares; these shares would be traded on state stock markets. Kornai believed that without private ownership, state entities owning these shares would continue to behave within soft-budget constraints (Kornai, 2007, pp. 500–504).

2.7.2. Proportions of the two kinds of dependency

Vertical dependencies predominate over horizontal ones, despite the growth of the latter. Coordination and control methods are altered but not fundamentally changed. There is a critical point at which bureaucratic intervention destroys market vitality, so the balance between them is not an arbitrary question.

The demeanour of managers assumes the appearance of their capitalist counterparts. They are not owners, but are granted rights of control over public firms, so their interests are not bound to the profit and net worth of the companies. Their positions are vertically dependent, 'one eye on the market and the other on their superiors, the important thing, in fact, is for the eye cast upward to see clearly: their present bonus or penalty and their future promotion depends on their superiors. The proprietor, if any, is the sum total of the bureaucracy. But this is 'intangible.' What was established about the classical system remains true: public property belongs to all and to none.' (Kornai, 2007, p. 505) An independent managerial class opposed to the bureaucracy and independent of the workforce fails to emerge. Managerial behaviour is governed by multiple roles: as intermediate managers dependent on their superiors, yet wielding local power; as recipients of residual income; as technocrats of production and development; and as representatives of employees' interests (Kornai, 2007, p. 505).

2.8. The rise of the private sector

The classical system defined the private sector as a vestige of capitalism. Leading reform Communists such as the CPSU general secretary Mikhail Gorbachev, declared universal public ownership as his objective as late as 1988, and CCP General Secretary Zhao Ziyang reiterated his faith in public ownership and its inviolability in 1989 (Kornai, 2007, p. 445).

Small-scale producers can develop into large-scale capitalists and unearned income and exploitation is an anathema to Communist ideology. Thus high-income earners become the object of envy and hatred. Wide layers of society, imbued with the ruling ideology, share this outlook and approve of measures taken against 'parasites'. The reform socialist ideology is an inconsistent combination, internally torn between the need for pragmatic solutions and antipathy towards the agents and methods of these solutions (Kornai, 2007, pp. 446–447).

Kornai regards the formation of the private sector as the most profound change in the economic sphere under reform socialism. Private sector growth mushrooms naturally and spontaneously as soon as there is a decrease in hostility towards it. It is driven by material incentives, a desire for autonomy, the satisfaction of self-mastery and a thirst for independence. And a part of the bureaucracy assists the private sector in order to alleviate shortages and to divert attention from political shortcomings (Kornai, 2007, pp. 432–435). Private owners establish new enterprises parallel to state sectors, or acquire ownership of state or collective assets through privatisation. The first method tends to characterize the reform era, but privatisation can also take place outside the productive sphere, for example in housing stock (Kornai, 2007, p. 444).

In Kornai's opinion there is an organic affinity between private ownership and the coordination of economic activity through the market. Private enterprises relate on a horizontal basis. They do not wield administrative power over one another. Individuals own property and voluntarily

engage in autonomously determined interconnections in conditions of decentralized coordination. Prices are the natural domain of the proprietor, as costs and sales are the means and measures of material gain. Unhindered entry into the market, competitive rivalry, and consequent failures, are all part of normal market conditions.

‘All economic relations arising among private enterprises or between them and the general public are coordinated basically by the market mechanism. A natural advance of the market mechanism is inseparable from the expansion of the private sector.’ (Kornai, 2007, p. 448)

Contact between the two sectors is fraught with conflicts. Private entrepreneurs dislike the privileged access of state enterprises to power and credit. State managers envy the autonomy of the private sector, and the fact that higher wages may ‘steal’ talented workers away from public firms. Workers in the private sector envy the security of public sector workers. Access to key materials may come only from public enterprises, so private companies often need to bribe officials to sell to them, and access to public sector contracts is restricted by the state. Fair competition does not exist, thus both sectors have legitimate grievances against the other (Kornai, 2007, pp. 505–507).

Hard budget constraints dominate the private economy; a failure to generate sufficient income and profits lead to survival crises for private enterprises. However, in reform socialism, bureaucratic coordination still dominates and impacts on the operation of private firms in a myriad of ways. This significantly differs from the interventionist state in capitalist countries (Kornai, 2007, pp. 448–449).

2.8.1. The private sector and the bureaucracy

The bureaucracy has a variety of interest groups within it. They relate to the private sector differently. The bureaucracy governs the public sector from within its administrative authority and experience. But in the exercise of power over the private sector bureaucrats operate outside of

their natural domain. This undermines the power of the bureaucracy. Although private sector economic activity develops spontaneously, so does bureaucratic opposition to it (Kornai, 2007, pp. 450–451).

The bureaucracy determines and defines the enforcement of the legal framework governing private operations, but the private sector seeks protection and guarantees for its property. The parameters of legal activity are amended, permitting previously forbidden activities, but this simultaneously extends bureaucratic authority over them. Other previously illegal spheres may now be tolerated, and semi-legal activities proliferate. New forms of dependence on bureaucratic leniency develop, as legal measures to enforce contracts are weak or non-existent. The state is protected against private sector interests by existing power, ideology and law. Tax rules are arbitrarily applied and the burdens imposed eat into profitability. The tolerance of grey markets fosters a moral climate of lawlessness in tax relations.

Limited access to bank credit, materials and state orders, discriminates against the private sector, which has no voice in political life. This ambivalent environment and insecurity, promotes short-term money making as the norm for private sector activity. Conditions of shortage permit private firms to disregard quality, and the bribery needed to engage in their business activities, promotes a cheating culture. This in turn increases public hostility to private entrepreneurs (Kornai, 2007, pp. 451–455).

Family based economic coordination increases in the reform era and creates a zone of privacy and independence from the state. Privatisation of housing promotes family ownership, engendering autonomy and positive identification with private property. The state also begins to retreat from welfare responsibilities (Kornai, 2007, p. 458). ‘Traditional’ family roles provide a retreat from the bureaucratic invasiveness of the past. This benefits state finances, whilst those dependent on subsidies, or unable to tap into the new sources of financial accumulation, become more impoverished. Women lose the independence provided by work

and may be burdened with a wide range of welfare responsibilities previously shouldered by the state (Kornai, 2007, pp. 458–459).

Kornai predicted that after the demise of socialism, the advance of the private sector would be all the more rapid where the private sector had already matured. Capitalism can be ‘abolished by state command’ in a relatively short time span, but the development of the private sector cannot be ‘performed by state command’ (Kornai, 2007, p. 460).

2.8.2 Interaction between the mechanisms; assessment of the changes

In the reform era, managerial flexibility is increased, the quality and quantity of products improve, new product innovation and production is accelerated, and buyers’ interests are considered more frequently. The rigidity of the economic atmosphere changes, and barrack like controls and fear, associated with the classical system, diminish.

The failings of bureaucratic and market mechanisms reinforce each other, producing a no-man’s land scenario where neither operates effectively. The old bureaucratic discipline is undermined and central power is no longer able to enforce policies, simultaneously, market discipline, governed by competitive rivalry is also absent.

Markets require a minimal trust level to develop ‘good will’ and avoid constant litigation. Instead of this, bribery, nepotism and ‘cheap commercialism’ predominate, and there is widespread petty theft of state property -as it is not endowed with ‘value in the public’s eyes.’ (Kornai, 2007, p. 509)

In the 1980s, the Chinese a ‘dual-system’ economy encouraged the sale of subsidized goods at higher market prices. Managers often pocketed the difference. Those with bureaucratic connections spawned entire industries based on ‘back-door’ access to these state subsidized goods. The general public viewed the new rich with profound dislike, unconcerned whether the wealth was a product of entrepreneurial

endeavour or theft. Hatred of corruption erupted in 1989, in a widespread social movement alienated by the results of the reform process (Kornai, 2007, pp. 509–510).

According to Kornai, the imaginable model of a rational, objective and neutral bureaucracy, behaving according to market impulses, was contradicted by the actual structure, surviving ideology and property relations, within which the attempts to create market socialism were made. He thinks that the main benefits of market-socialist experiments are that they shake belief in the command economy, promote spontaneous forms of economic activity, and improve the public perception of private enterprise and the market (Kornai, 2007, p. 511).

2.9. Conclusion

This chapter is a presentation of the central concepts and definitions of Kornai's socialist system, particularly reform socialism. Kornai's systems' theory examines the rise and fall of two specific types of socialism. The basic features of these socialist systems were shaped by the backward state of the pre-revolutionary society. The objective to catch-up with the advanced capitalist countries is shaped by ruling ideology and by social pressures to raise living standards.

The political system acquires the form of a dictatorship, which is all-encompassing and brooks no organized opposition. The reform socialist system maintains control over political power, armed force, and the appointment of leaders in bureaucratic agencies. However, the system becomes unstable because its internal coherence disintegrates, as the tolerance of dissent and private economic interests at the margins, undermines the internal consistency of the ideology and mission of the Party and bureaucracy. The emergence of private economic actors plays an important role in weakening the hold of state owned entities over the economy.

The loosening of command and control systems inside the bureaucracy undermines its unity and increases the scope for bureaucratic jostling and bargaining as well as for pressure from the workforce that finds expression in populist tendencies amongst managers and officials in relation to their base constituency. The system of bureaucratic planning continues to coordinate the economy under reform socialism but now private firms operate alongside state enterprises. Investment hunger and forced growth are default policies of the bureaucracy. A drive for rapid development encourages an untamed obsession with growth and this also leads to the pursuit of medium to long-term megaprojects. This produces patterns of growth that swallow-up investments and resources and generates unique cycles of expansion and slowdown. These are connected to the tempo of planning cycles and the limited resources available to realize bureaucratic investment plans.

The inconsistency of the system finds expression in clashes between different interest groups and policies. This undermines ideological authority and produces internal contradictions within the ruling party and society. The tolerance of markets undermines planning and increases the influence of private incentives and private businesses. The weakening of central authority undermines planning but fails to nurture adequately functioning market entities, or mechanisms that might otherwise provide the basis for an alternative system. The system becomes unable to satisfy societal demands, the demands of private business, and the demands of various bureaucratic interests. Eventually this gives rise to a revolutionary crisis that brings down the system as a whole.

¹ Kornai is aware that the term socialism is contested as an appropriate definition for the states that he studies, but argues that various socialist schools will find common attributes of socialism present in such societies. The main point of Kornai's analysis is to identify and abstract the fundamental trends and features of the specific system that ruled many countries in the 20th century in the name of socialism. Kornai identifies 26 countries as socialist in 1987, encompassing 34.4% of the global population (Kornai, 2007, pp. 6–11)

² Kornai offers the following list of countries: the Soviet Union, Albania, Yugoslavia, China, Vietnam, Cuba, Congo, Somalia, South Yemen, Benin, Ethiopia, Mozambique, Nicaragua and Zimbabwe (perhaps a rather odd addition by Kornai). In all of these examples the background to their revolutions was wars, civil wars and anti-colonial liberation wars. See (Kornai, 2007)

3. Is China still socialist?

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3.1. Introduction

Kornai's approach to socialism is based on his study of the systems that ruled over a third of humanity in the twentieth century. This chapter addresses the main question of this thesis: 'Is China still socialist?' This is evaluated by examining the degree to which China's system corresponds with Kornai's definition of socialism. I assess contemporary Chinese political economy using the tools developed in *The Socialist System* (Kornai, 2007). However, Kornai's writings on China since 2008 define China as capitalist (Kornai, 2008, 2014, 2016). This assessment is considered in greater depth in chapter 4.

I select Kornai's three main definitional criteria for socialism and examine the related evidence on China. They are: Communist Party control of political power and Marxist ideology; the dominance of public ownership of the commanding heights of the economy; and the dominance of bureaucratic coordination of the economy.

To undertake this task I evaluate an extensive body of research, which provides evidence from a diverse range of multi-disciplinary sources. This draws on cutting edge research by leading scholars of Chinese economic history, comparative political systems, political science, public administration and management, sociology, political economy, demography, economic geography, and urbanization studies. In addition, I cite from documents and speeches from the Chinese government, government economic statistics and census data, as well as quality journalism from the Chinese and Western media.

3.2. Kornai's connection to the Chinese debate on reform

In 1985 leading Chinese economists and policy-makers attended a unique conference held on a boat travelling the Yangze river. This was called the Bashan Boat Conference. It brought together eminent Chinese reform minded economists and a wide spectrum of foreign economists to engage in an intensive deliberation on economic reform in 1985. One of China's most prominent economists Xue Muqiao introduced the conference as being about economic planning and macroeconomic management. China's price system, the relationship between plan and market, the rate of growth, and the nature of reform were all on the table for discussion. János Kornai's presentation was the most influential and challenging for the Chinese audience.

Kornai impressed his audience by focusing on the experience of state owned firms in Hungary. He examined their vertical dependence on bureaucratic superiors and their horizontal relations to consumers. His presentation and assessment of these questions struck the Chinese audience because it was intimately connected to their own discussions and concerns. The Keynesian economist James Tobin warned that China's economy was overheating and recommended contracting monetary policy and a slower rate of growth. However, some of the core language used by Tobin lacked an intellectual or linguistic affinity to the

history and structure of Chinese economic discourse (Gewirtz, 2017, pp. 136–145).

By contrast the Chinese audience easily grasped Kornai's presentation. When he discussed the economic problems of reform socialism, he dealt with problems that his audience were familiar with from first hand experience. His presentation dealt with administrative and market coordination. In his view, administrative policies could take the form of direct or indirect regulation, whereas market coordination policies could be based on free markets, or markets governed by macroeconomic control. The last type, markets governed by macroeconomic control was what Kornai wanted his audience to concentrate on. This offered a means to tighten the budget constraints of enterprises, and to simultaneously protect important firms that might find themselves in serious difficulty. The more price sensitive the response of enterprises the better. Kornai's suggestion had the advantage for Chinese economists that it could easily fit within the official 'planned commodity economy' designation that was adopted by the Party in 1984 (Gewirtz, 2017, pp. 146–149).

3.3. Kornai's rejection of China as a socialist system

Today, Kornai categorizes China's system as Leninist in only one sense: that the Communist Party retains its exclusive political monopoly and continues to repress opposition. However, he maintains that the party has changed its ideology and adopted a positive view of capitalists, private property and the market.

The 'ownership structure has undergone fundamental changes, in which the state-owned sector has given up its leading role. The role of bureaucratic coordination and central management has been drastically reduced and largely replaced by the market. China is not a classical socialist system, and is closer to a typical capitalist system.' (Kornai, 2008, pp. 58–59)

Thus Kornai argues that the Communist Party underwent a metamorphosis over decades, in which, the ideology of socialism was abandoned, and public ownership and bureaucratic control, also underwent a fundamental transformation (Kornai, 2008, pp. 147–150). He maintains that public ownership has radically declined and private ownership now predominates. ‘The first characteristic of capitalism –a dominant role for the private sector –either applies or is near to applying.’ (Kornai, 2008, p. 148) The statistics cited by Kornai reveal that 60% of the value added to the national economy, derived from the private sector in 2005 (Kornai, 2008, p. 149). As we shall see, the statistics on this question are sharply contested, and this makes assessing the relative weight of different ownership forms problematic. Furthermore, I will show that his methodology developed in *The Socialist System* better contextualizes the hierarchy of ownership and power in contemporary China, and elicits a more precise picture of the relative weight and influence of the private and public sectors.

The dominance of market price transactions is cited as evidence that the ‘second characteristic of the capitalist system – predominance of market coordination –clearly applies’ (Kornai, 2008, p. 148). Although Kornai placed significant emphasis on planned prices in socialist systems dominated by bureaucratic coordination, he did not previously elevate generic bureaucratic prices to the definitional determinant of the dominant mode of coordination.¹ Kornai suggests that market socialist experiments in the reform era attempt to adjust prices by market methods, whilst maintaining bureaucratic coordination and control over factor prices (Kornai, 2007, p. 525). His contention was that bureaucratic coordination within a market socialist environment distorts true price signals, as it operates through soft budget constraints and maintains the close relationship between the party, bureaucracy, public banks, publicly owned companies and other state entities (Kornai, 2007, pp. 512–527).

Kornai believes that the CCP has abandoned its outright hostility to private property; and Party cadres and business interests have intermingled within an authoritarian system. Although, the formal political

structures of the socialist system remain, its ideological content has been jettisoned and replaced with a purely rhetorical allegiance to socialist and communist ideas (Kornai, 2008).

3.4. The organization and ideology of the Chinese Communist Party

The Chinese word for the Communist Party is *gongchandang*; literally translated this means the “public assets party”. Indisputably, the CCP exercises a monopoly on political power and dominates the government and state apparatus. Its 86 million members (2013) are organized in 4.3 million grassroots party organs.² Some 85% of party members work for a state entity or for the party.³ Members must abide by the constitution and policies of the party, and should participate in their party branches, cells or units. Party cells operate in all official and semi-official state entities and nearly all legally registered civil society organisations. The party also extends its reach into the private sector. In 2012 over 300,000 party committees existed in 210,000 large private entities.⁴

David Shambaugh’s book *The Chinese Communist Party: Atrophy and Adaption* (Shambaugh, 2008) is a study of China as a ‘Leninist party state’. It uses comparative methods to study assessments of why Leninist states collapsed in Eastern Europe and the Soviet Union, and it considers why the CCP survived.

Shambaugh examines both Western and Chinese assessments of the causes and consequences of the systemic collapse. The Chinese Communist Party leadership was initially stunned, and blamed Western plots to promote “peaceful evolution”. However, by 1990 they considered a more complex mixture of reasons. The Chinese Academy of Social Sciences (CASS), the Central Party School, and Marxism and Socialism Institutes, began a research and analysis process that continued until 2004.

Shambaugh observes that the leadership’s view of Soviet reforms was one of skepticism between 1986-7; support from 1987-9, suspicion

between 1989-91, shock in 1991-2. Then, they engaged in a systemic study between 1993-2004, and drew their conclusions in 2004-5 (Shambaugh, 2008, p. 55).

Chinese research involved a broad historical overview of the ossified character of the Soviet Party. Some argued that this became entrenched under Leonid Brezhnev, the Soviet leader from 1964-1982, and believed that had the reform policies carried out under Nikita Khrushchev in the period 1953-1964 continued, the crisis and collapse in 1989 could have been avoided. Chinese Party scholars studied the way that a wide spectrum of oppositional civil society forces emerged to overthrow Leninist states.

Reforms to the CCP's methods of governance were designed to prepare for all of the eventualities that triggered the collapse of other socialist systems, and to ensure its longevity and the reproduction of its power. The assessments that informed the analysis spanned a wide variety of governmental and economic systems around the world. The objective was to assimilate beneficial elements from any and all relevant systems. Official conclusions were published at the Fourth Plenum of the 16th Party congress in 2004. Shambaugh considered this meeting to be the most important since 1978, when Deng Xiaoping initiated China's reforms.

Shambaugh's book provides a strong counter-weight to Kornai's concept of a fundamental and irreparable ideological degeneration within the Party. He shows that Party intellectuals and advisors undertook a broad, sweeping and sophisticated analysis of the reasons behind the collapse of the Soviet Union and other socialist states. This undertaking was notable for its depth, its holistic character, and its attempt to contextualize the collapse in broad historical terms.

Of particular interest was the Chinese assessment of the former Soviet leader Michael Gorbachev. In Western scholarship, he was almost universally credited with bringing down the system. However, this was

not the dominant Chinese theory. Indeed, many Chinese studies concluded that Gorbachev's main 'error' was to carry out political and economic reform simultaneously. Indeed, most Party scholars claimed that the collapse of their sister parties was rooted in long-term dysfunctional and systemic problems (Shambaugh, 2008, p. 70).

The Party leadership decided to carry through reforms to the Party's methods of governance. They wanted to prepare for all of the eventualities that triggered the collapse of other socialist systems, and tried to reconfigure the Party's 'governing capacity'. China's 2800 Party schools, that train party cadres about a broad range of governance systems and tasks, are singled out by Shambaugh as they sought to sustain Party rule by broadening feedback systems to allow Party and state agencies to head off any discontent that might escalate into a systemic crisis. The conclusions drawn by the CCP's researchers were quite complex, but they consistently focused on key issues which it was felt, unless learnt from, would lead to similar events in China and the loss of power by the Chinese Communist Party.

They blamed the Soviet Communist Party's demise on four main causes:

1. Economic deterioration
2. Too much distance between the ruling parties and the masses, and a lack of local party building
3. The failure of the trade unions to act as a bridge between the working class and the party, and
4. Western activities to promote peaceful evolution (Shambaugh, 2008, p. 50).

Following this period of studying what happened to the USSR and Eastern Europe, the Chinese Communist Party undertook a full scale "rectification campaign", which lasted for 18 months and ended in July 2006. During this time all 73 million members of the Chinese Communist Party had to 1. Undertake three months of study of classical Marxist texts, some of Mao's writings and some speeches by present day leaders

(during this period no party members were allowed to leave China)
2. Spend three months writing self-criticism and three months circulating this to colleagues
3. Then spend three months being criticized by colleagues and then rewrite their self-criticism (Shambaugh, 2008, pp. 129–130).

Shambaugh's study contradicts Kornai's view that China's leaders employ socialist and Marxist phraseology in a merely ritualistic fashion, and not out of conviction. He writes that although a 'strong case can be made that Marxist-Leninist ideology and its various Chinese permutations are irrelevant in today's China – or are an impediment to any real CCP reform. The logic of this argument is that, like socialism or communism as political-economic systems, Marxist-Leninist ideology has little analytical or policy relevance in the twenty-first century world. Indeed Marxism-Leninism is considered a hindrance to modernization and incapable of explaining contemporary phenomena like globalization. The CCP, however, does not and *cannot* agree with this judgment – for the very reason that it is a communist party.'

(Shambaugh, 2008, p. 104)

This certainly appears to correspond with the views of President Xi Jinping. For example, at a group study session of the Politburo held on 29 September 2017, he stated:

'Marxism is the foundation for advancing the cause of the CCP and the people, and the source of their strength to make progress. Should we deviate from or abandon Marxism, our Party will lose its soul and orientation. We must follow the guidance of Marxism, a faith unshakable at all times and in all circumstances.'

(Xi, 2017, pp. 68–69)

3.5. CCP organization and state power

The CCP is certainly organized in a way that corresponds fully with Kornai's original description of communist parties. Debate and discussion

inside the party is followed by uncritical compliance to implement party policies and directives. However, where decisions leave scope for interpretation, local committees can, and do, amend, adjust and resist party policies. However, in cases of intransigence, work teams are dispatched to enforce directives (Lawrence and Martin, 2013, p. 6).

Xi Jinping is General Secretary of the Party and Chairman of the Party's Central Military Commission. The Politburo and its Standing Committee constitute the leadership of the party and are elected by the Central Committee (CC).⁵ The current CC has 205 full and 171 alternate members. In 2007 the CC informally voted on 200 candidates before identifying the final 25.⁶

The party commands 2.5 million members of the People's Liberation Army, 1.5 million members of the People's Armed Police, and 800,000 members of various internal security services. Approximately 60% of soldiers and police officers are party members (Bruce J. Dickson, 2014, p. 52). Recently, Xi Jinping reiterated that, 'the Party commands the gun'.⁷

The Party's own bureaucracy is dominated by four agencies:

- The Central Discipline Inspection Commission: the party's anti-corruption agency.
- The Organization Department: which recruits, trains, and assigns personnel to a vast range of party, state, and public organizations.
- The Propaganda Department: which deals with ideological and media work.
- The Central Commission of Politics and Law: which controls internal security agencies (Lawrence and Martin, 2013, pp. 24–25).

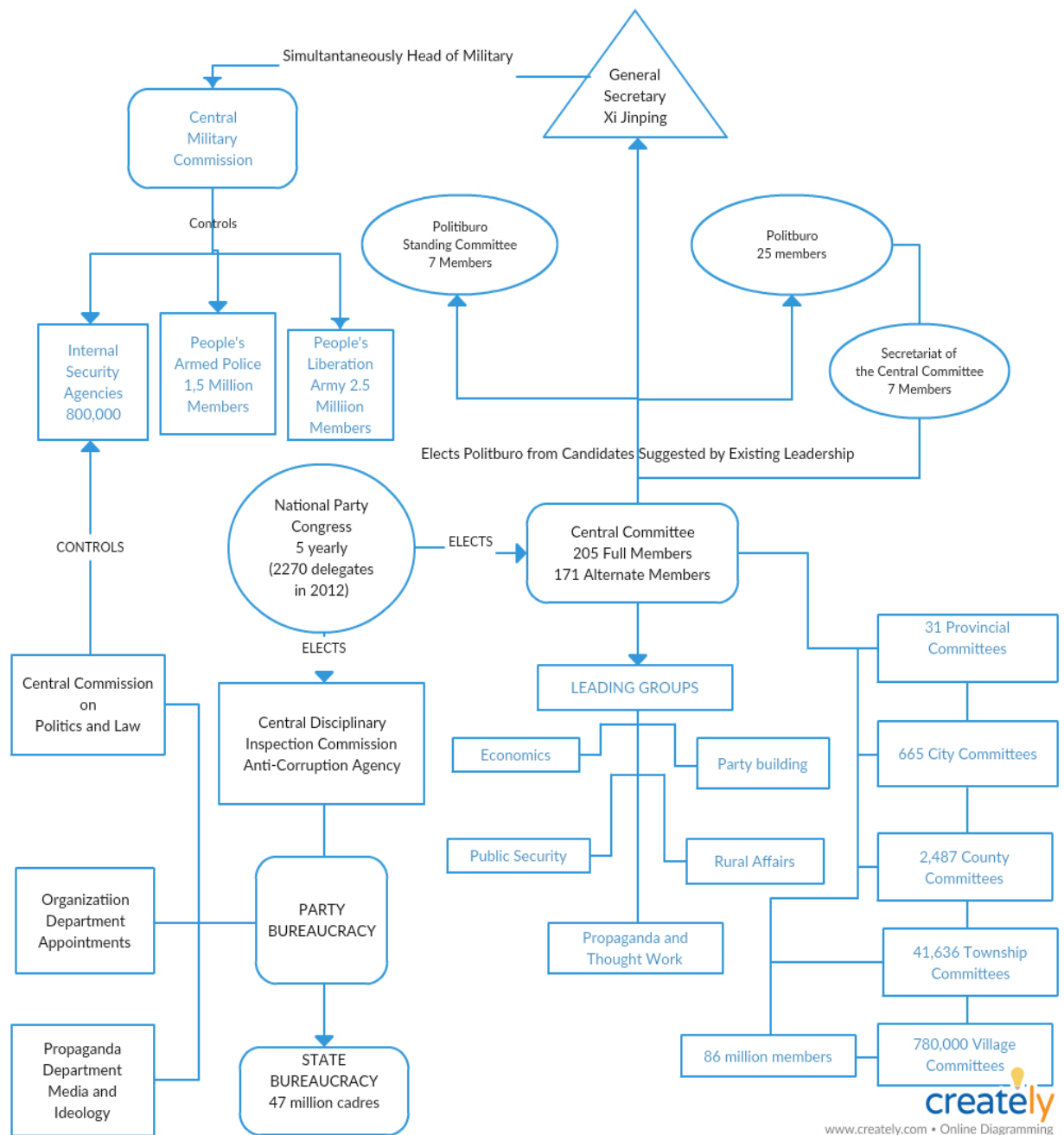


Figure 2. Chart outlining the structure of the CCP and its internal bureaucracy

After the 1970s state administration was devolved to state agencies. However, Party committees mirror state organisations at all levels, and make all major decisions. 'Cadres' in China's are public officials in

responsible or managerial positions in the party or government. Cadre appointments are made by the Central Organisation Department of the Communist Party through its nomenklatura system - a list of leadership positions and suitable candidates. State organisations and work units are hierarchically ranked according to military principles. The promotion, rotation and transfer of officials occur across and between political, economic and state institutions. This generates loyalty to the party and state rather than to one's particular employment, shareholders, or private interests (Lin, 2011, p. 76).

Positions at the upper levels of the hierarchy are all political appointments. The central party and state, vertically controls local governments through the power to set objectives and targets, and can remove those displaying disloyalty or too much independence (Lin, 2011).

3.6. The Central Organization Department

The executives of the top SOEs and banks are appointed by, and beholden to, the Central Organisation Department of the CCP. This means that the goals of the state override shareholder value and the pursuit of profit maximisation (Andrew Szamosszegi & Cole Kyle, 2011, p. 3). The Central Organisation Department (COD) recruits, appoints, evaluates, promotes and removes, party and governmental officials at central, regional and provincial levels. The COD keeps detailed files on all employees of the party, government, state enterprises, the judiciary, the mass media, and state entities and institutions. This facilitates universal control over personnel of the state. In addition the personnel files of urban workers employed by the state are stored under party control and are secret and intrusive. This mechanism is typical in the socialist system. Employment transfer depends on the transfer of your personal file. This acts as a critical mechanism of control. Similar organisational supervision and control also extends to large private sector entities where party committees exist. However, in private and foreign owned entities the personnel files are less critical, and the party

may operate under the auspices of a trade union in these companies (Lin, 2011, pp. 72–73).

Government employees do not have to be party members, even at a ministerial level, but party members perform nearly all-sensitive roles. In 1997 China had 40.19 million cadres, of whom, 15.27 million were CCP members, and 24.91 million were not (Heilmann and Kirchberger, 2000, p. 2). It would seem logical for the size and influence of the bureaucratic state to decline when the market mechanism replaces planning as the central coordinating force, but the reform era witnessed a major expansion in the number of officials on the government payroll, from 20 million in 1990 to 46 million in 2004. This rose to 47.78 million in 2005, divided between 891,000 units (Ang, 2012, p. 692).

Non-party cadres have been a traditional recruitment field for the party. At the top level of the bureaucracy: ranked above the level of a county/division chief, there are approximately 500,000 cadres. Over 95% of them are party members. For these cadres, the obedience of party and non-party cadres is a prerequisite for the reproduction of their power. However, ordinary party members do not constitute part of the elite, although they commonly work in supervisory roles or as group leaders. Walder believes that these relationships constitute the only real social base of the regime (Andrew G. Walder, 2004, pp. 196–197).

Party members are permitted to express their opinions inside party structures and, in the process of developing policies, party leaders engage in wide ranging policy debates in which experts and the public are invited to make contributions or comments. The party is able to use its control over the mass media to shape public opinion to serve its objectives. As officials serve limited terms and their roles are rotated they need to be sensitive to popular opinion. However, as external supervision and control is lacking, the danger of rent seeking behavior and insider jostling for control of resources and revenues is ubiquitous. So it is hard to tell whether those seizing control of revenue streams are in command, or whether central objectives and planning edicts are the driving force

behind China's modern economy. Naughton concludes that dominant insider interests should be understood in a broad sense as 'those of a larger group of Communist Party officials, politicians and technocrats, and even the urban population - at least those with urban residence permits - as a whole.' (Naughton, 2017, pp. 20–21)

The National People's Congress (NPC) is China's highest organ of state power. It exercises legislative and constitutional power, elects government leaders and ministers, supervises planning, and makes decisions on war and peace.⁸ Within the NPC system there is some scope for limited expression of opposition. Anyone with the support of 10 other voters can stand in direct elections to lower level People's Congresses. In practice, this provokes sanctions, repression, and harassment. Nevertheless, independent candidates stood for election and won seats in Beijing, Changsha, Chongqing and Chengdu as far back as 1980 (Yuan, 2011, p. 391), and estimates for the number of independent candidates in 2006 ran as high as 10,000 (Yuan, 2011, p. 393). These candidates are commonly grassroots heroes; lawyers, victims of power-abuse, idealistic social activists, or political dissidents (Yuan, 2011, pp. 395–396).

Premier Li Kejiang presides over the State Council. All major institutions and working organs of the state are subordinate to it.⁹ Ministries and Commissions are bureaucratic entities, which formulate relevant regulations and help to draft laws. They can affect, amend and adjust policies, and interpret their implementation (Lawrence and Martin, 2013, pp. 28–31).¹⁰

A large number of organisations participate in policy formulation, debating proposals and generating ideas. They include the Central Party School, Leading Small Groups, numerous think tanks, research organisations and institutes, as well as academia, the mass media and China's Internet users, known as netizens.

3.7. Ownership and control of the ‘commanding heights’

Kornai says that the majority of China’s GDP comes from the private sector. This shows that the ‘first characteristic of capitalism –a dominant role for the private sector – either applies or is near to applying’ (Kornai, 2008, pp. 148–149).

The state owned enterprise is the core of the political economy of socialism. According to Kornai, it is ‘the first and most important property form’ of the socialist system. It occupies what Lenin called the ‘commanding heights’:

‘the positions that allow the other, non-state sectors of the economy to be dominated: mining, energy production and manufacturing, transport, domestic wholesale trading, foreign trading, banking and insurance. On the other hand, agriculture, retail trading, and other services to the general public, do not qualify as ‘commanding heights,’ and although state firms appear in them, other property forms occur alongside and may even predominate.’(Kornai, 2007, p. 71)

It is certainly true that Lenin regarded ownership and control of the commanding heights of the economy as an essential prerequisite for socialism.¹¹ And Kornai accepts Lenin’s concept of the commanding heights as his definitional determinant of the dominant form of ownership over the means of production. Indeed, although the objective of Marx and Engels was to abolish private property in production, and this was a ‘cornerstone of the ideology’ (Kornai, 2007, pp. 444–445). A subtlety in their tactical approach was evident as far back as 1847, when Engels wrote in ‘The Principles of Communism’:

‘Will it be possible for private property to be abolished at one stroke? No, no more than existing forces of production can at one stroke be multiplied to the extent necessary for the creation of a communal society. In all probability, the proletarian revolution will transform existing society gradually and will be able to abolish private property only when the means of production are available in sufficient quantity’.¹²

Under Kornai's socialist political economy the Communist Party controls the state, the leading publicly owned financial institutions, and a broad range of state enterprises. This permits the mobilisation of resources to implement plans. From this perspective, the power derived from ownership and control of the commanding heights in China's system is certainly highly concentrated and amplified.

Let us examine the extent of public ownership in contemporary China:

The state sector is divided into three parts.

- State owned enterprises (SOEs) run by the State-owned Assets and Supervision Administration Commission (SASAC) under the State Council.
- SOEs run by local SASACs under lower government tiers.
- SOEs controlled by other SOE owners and enterprises that are owned and controlled through SOE subsidiaries.

The national SASAC was formed in 1999. It now supervises 121 Central State Owned Enterprises (CSOEs). It has its origin in the mid-1990s when Asset Management Companies (AMCs) were formed by China's four state owned commercial banks in order to off-load bad loans. AMCs were supposed to make SOEs act in a more market responsive fashion.

In 2006, the Chinese government published a list of 'strategic' industries that it deems vital to national or economic security and that will remain permanently in state hands. They are defence, power generation and distribution, oil and petrochemicals, telecommunications, coal, aviation and shipping. In 2007, this list was extended to include shipbuilding, metalwork and construction, and fifty non-financial enterprises are deemed to be 'strategic'. They act as the commanding heights of the state sector. Provincial governments use the same terms of reference as the central state to identify enterprises that must remain in state hands (Chan, 2009).

The state will also retain significant or absolute control over those sectors defined as 'pillar' and 'basic'. These are machinery, automotive, IT, construction, steel, base metals, chemicals, land surveying, and R&D. Other sectors in which significant ownership stakes and control are to be maintained include, trading, investment, medicine, construction materials, agriculture, and geological exploration (Mattlin, 2007). In addition the government is increasing its share ownership in those sectors it defined as 'key' and 'pivotal', but these categories are fuzzy and are subject to political and bureaucratic pressure.

Although foreign mergers and acquisitions are allowed to encroach on state ownership, and the purchase of existing enterprises holds an attractive appeal for foreign investors, blocks on foreign investment outside the least prioritized sectors are commonplace. Even where local bureaucracies favour such outside investment, central bodies, particularly the Ministry of Commerce (MofCom), flexibly interpret their definition of the importance of those companies in order to block mergers and acquisitions. The criteria used by MofCom to review potential monopoly dangers are set at a relatively low benchmark. They are defined in terms of assets, revenue and market share, or by the number of enterprises in which investors hold stakes; resulting in greater restrictions on foreign investment and increasing selectivity over project approvals (Mattlin, 2007).

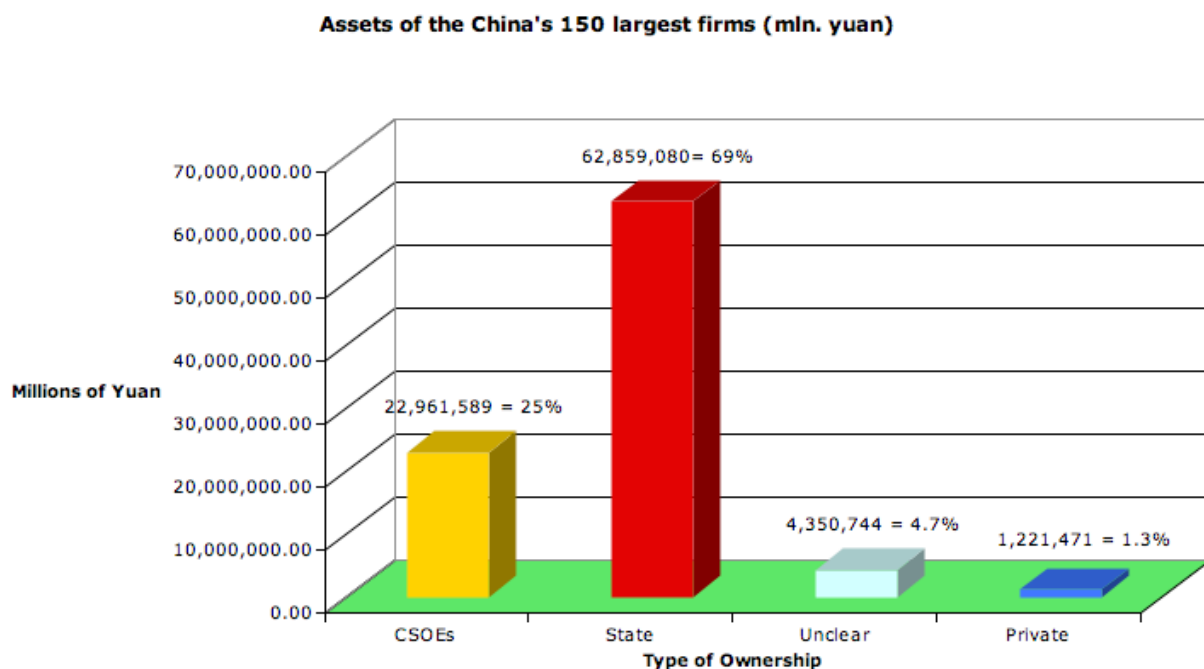


Figure 3. Chart showing the assets of China's 150 largest firms in 2010

The above chart shows the assets of China's largest 150 companies in 2010 (as measured by revenue). The combined assets of these 150 companies made up 84% of the largest 500 companies. The assets of the largest 117 state owned companies within the top 150 firms were equal to 41.2% of China's total corporate assets. Yet, according to the Economic Census in 2008¹³ there were 4.95 million registered corporations in China¹⁴ with total assets of 207,800 billion yuan (including domestic, Hong Kong, Macao or Taiwan invested (HKMTI), and foreign invested).

Key to chart:

- CSOEs: refers to central state owned enterprises
- State: refers to state enterprises owned by local government or state institutions
- Unclear: refers to firms where I was unable to ascertain the predominant ownership status
- Private: are firms that are predominantly privately owned.

The data is from 2010 and was published by China.org.cn¹⁵ and the All China Federation of Industry and Commerce.¹⁶

A 2015 survey by the OECD on the role of State Owned Enterprises presents ‘the most comprehensive and internationally comparable dataset currently available on the size, sectorial distribution and corporate forms of national SOE sectors in 40 countries’ (“The Size and Sectoral Distribution of State-Owned Enterprises | OECD, p. 7). These SOEs are defined by the fact that they offer goods and services in markets that could otherwise be carried out by profit seeking private enterprises (“The Size and Sectoral Distribution of State-Owned Enterprises | OECD, p. 11).

The dataset of 40 countries includes: China, India, Brazil, the UK, the USA, France and Germany. China stands out like a sore thumb in terms of the size and weight of its SOEs compared to all the other countries combined.

- There is a combined total of 2,467 of such SOEs in all 39 countries other than China. They are valued at over US \$2.9 trillion, and employ 9.2 million people in total.
- According to the OECD’s categorization method, China has 51,341 central government owned SOEs.¹⁷ Their value is US \$29.2 trillion, and they employ over 20 million people. India’s SOEs by contrast employ 3.3 million people and their total value is just US \$338.5 billion, this comes in a distant second behind China.

The vast scale and combined resources of Chinese SOEs, means they can undertake global takeovers to acquire technology and knowhow; secure scarce resources from other countries; and undertake state financed and supported megaprojects such as the Belt and Road Initiative that aims to link together the road, rail and maritime infrastructure of 60 countries. It has been estimated that investment in related projects that are planned or already underway will exceed \$900bn.¹⁸

3.7.1. The invisible hand of the state

In the late 1980s, some advocates of market socialism in Hungary, Poland and China proposed the creation of stock markets where the shares of public enterprises could be bought from the state by various public entities. This was intended to foster greater fluidity and flexibility of response to market impulses. Kornai predicted that such firms would not change their behaviour as 'there cannot be a real market in capital without capitalist private owners' (Kornai, 2007, pp. 503–504).

When stock markets were formed in Shanghai (1990) and Shenzhen (1991) there was a rapid decline in the state shareholding of listed companies. However, the fall in state ownership directly corresponded to a rapid rise in institutional ownership by the state. This means that state-owned entities buy shares in these companies, although this often also implies that a portion of company shares may end up in the hands of managers or officials. However, this transfer of shares did not change the quantity of state ownership at all (J. Wang et al., 2011).

In the early 1990s the transformation of enterprises into corporate share based structures opened the possibility to trade shares and raise capital. A general audit was conducted which identified the assets and subtracted the liabilities of enterprises. This determined the net asset value of these enterprises, which was denominated in shares. Control over these SOE's assets fell to parent companies and the heads of supervisory agencies. Shares were divided between tradable A-shares and non-tradable state shares. Non- tradable shares were designed to stop wholesale privatisation whereas A-shares would be floated. In the 1990s the main concern was the potential to use A-shares to raise money, and to contain the danger that speculative fluctuations could undermine stability. The China Securities Regulatory Commission (CRSC) took central control over the exchanges, the market press, listings, and administrative controls. Attempts to sell a percentage of non-tradable shares, to raise revenue for state spending, hit the value of A-shares, as greater supplies would be issued without increased demand.

In the early 2000s the state intervened to prop-up the market and proposed measures to draw in foreign capital (Carl E.Walter in Oi and Walter, 2011, pp. 210–234).

Privatisation has never been a state policy, but widespread insider privatisations of small SOEs reduced the total number of SOEs from 250,000 in 1995, to 127,000 in 2005 (Mattlin, 2007, p. 25). However, according to Wang it is 'naïve to view the state as simply having divested itself from ownership of the state sector. Virtually all of the figures that scholars and the popular press have picked as evidence of the declining role of the state, relates to the decline in state shares but ignores the rise of institutional shares.' (J. Wang et al., 2011, p. 9) In 2004, the state was the largest shareholder in 70% of listed non-financial firms, which are commonly defined as private companies (Andrew Szamosszegi & Cole Kyle, 2011, p. 10).

The transformation of SOEs into share-holding firms took several forms, shareholding cooperatives, jointly owned enterprises, limited liability corporations and limited shareholding corporations. These firms held over 50% of capital assets and generated 35% of national sales. They replaced SOEs as the dominant public sector employers in the interior of the country. These hybrid forms were supposed to operate under hard budget constraints (Lin and Hu, 2011, pp. 725–728).

The introduction of stock markets in China appeared to represent a qualitative symbolic transformation toward capitalism. However, in July 2015, a crisis in the stock market revealed the inner contradictions between market pressures and state control and exposed peculiar features of China's markets. Formally, all the institutions, organisations, administrative and legislative forms that are required to replicate Western stock markets exist. However, Walter notes that despite such appearances: 'all aspects of the capital markets remain owned by some agency of the state' (Carl E.Walter in Oi and Walter, 2011, p. 238). As a consequence, when share prices began to collapse in July 2015, state banks were told to lend US \$209bn to the wholly state-owned China's

Securities Finance Corp in order to buy stocks. Market volatility was thereby contained by massive state intervention.¹⁹ Thus, the valuation and fate of these listed companies is determined on the basis of soft budget constraints.

Shareholding companies that mask their state ownership through stock market listings, help to generate a general underestimation of the extent of public ownership. In addition, it is also commonplace to ignore the role of the state in joint ventures with foreign invested enterprises (FIEs). These foreign investors include cases where state enterprises acquired FIE status by registering outside the mainland in order to gain access to FIE concessions. Indeed, even nominally private companies may conceal significant state share ownership in China.²⁰ However, the widespread underestimation of the influence of state ownership in the economy is not simply a question of misidentifying concealed public ownership relations, but also of understanding the 'dynamics of control' exercised by organs of the party and state (Andrew Szamosszegi & Cole Kyle, 2011, p. 25).

The System of Control over the Commanding Heights of the Economy

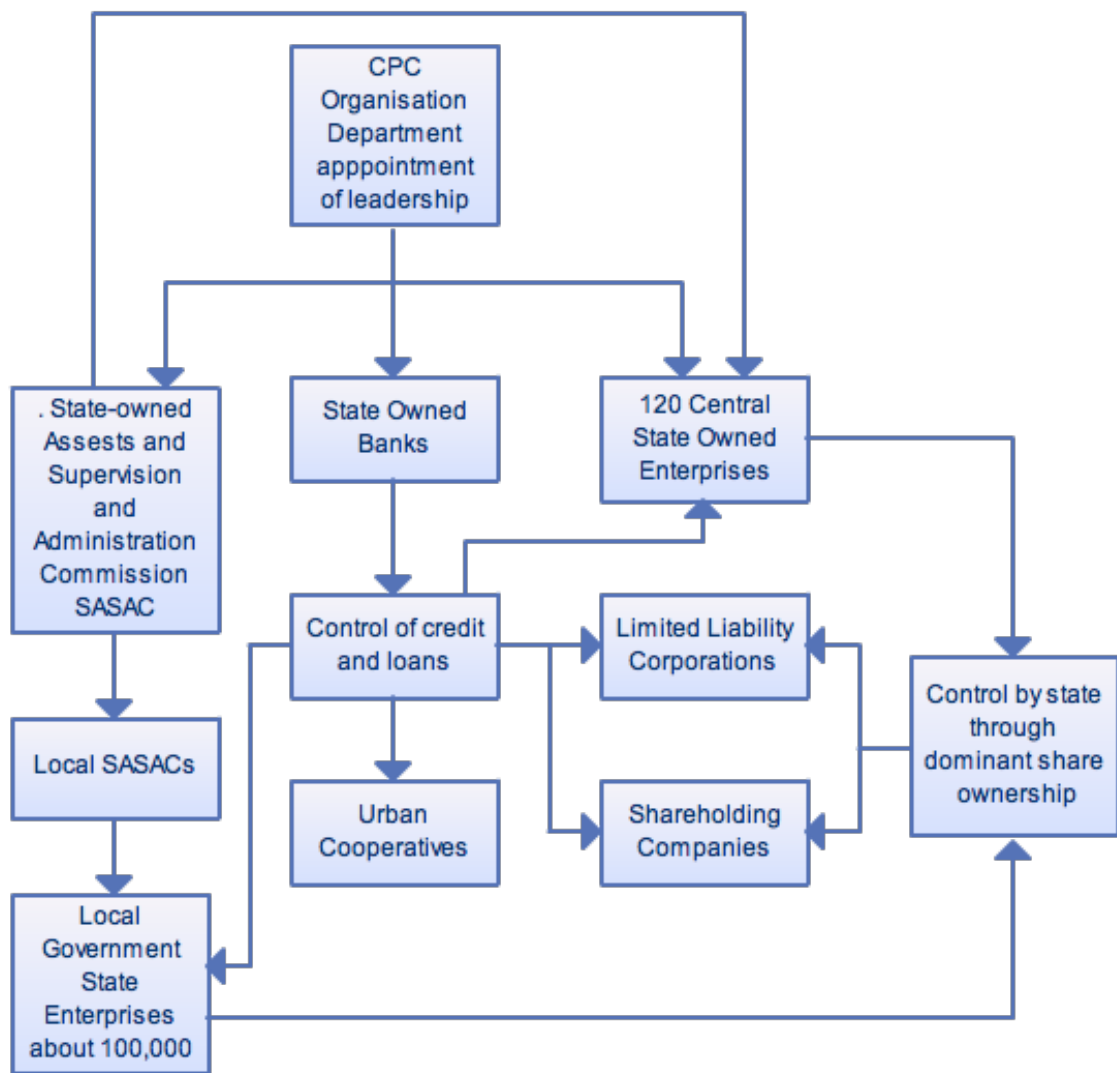


Figure 4. Chart illustrating the system of control over the commanding heights of the economy

The above chart shows the overall networked chain of command over urban state owned and state controlled enterprises. The organisation department of the Communist Party appoints the heads of the SASAC and the top 50 centrally managed SOEs. Most leadership positions in SOEs and banks are also party appointments. The SASACs appoints the managers and supervises SOEs at a national and local level (Andrew Szamosszegi & Cole Kyle, 2011, pp. 72–76). SOEs also exercise control over Limited Liability Companies and Shareholding Companies through dominant share ownership. State banks provide credit to SOEs at a

national and local level, as well as to Limited Liability Corporations, Shareholding Companies and Urban Cooperatives.

In his ground breaking book *Capitalism with Chinese Characteristics* Yasheng Huang (Huang, 2008) argues that the key to identify state ownership is control rights. Who can appoint the managers, dispose of the assets and determine the strategic direction of the firm? This information is hard to decipher from the datasets used to assess the extent of state ownership of Chinese industrial enterprises. Huang illustrated the problem by examining a widely cited study by the Organisation for Economic Co-operation and Development (OECD) about the extent of private ownership in China's industrial firms (Dougherty and Herd, 2005). Huang pinpoints the categorisation of legal person shareholding firms as problematic.

If you accept that they are private, then the foreign and indigenous private firms share of China's industrial profits was 28.9% in 1998, and 71.2% in 2005. However, if legal person shareholding firms are not counted as private, then foreign and indigenous private firms share of China's industrial profits declines to 17.6% in 1998, and 39.8% in 2005 (Huang, 2008, pp. 14–16)

As regards the percentage of GDP produced by each sector, similar problems exist when trying to identify what is a private or state owned firm. A comprehensive survey by Andrew Szamosszegi and Cole Kyle (2011) agrees with Huang (2008), claiming that the state sector is far more influential than the previous consensus believed. Although I agree with their view, the emphasis here is placed on the multi-spectrum character of party control that operates in systems that Kornai defines as socialist. So, although the statistical evidence is important, the hierarchy and mechanisms of control under socialism inevitably multiply the specific weight of state ownership within the economy and society.

Kyle notes that: 'The observable SOE sector under reasonable assumptions accounts for nearly 40 percent of China's economy. Given

additional information on the prevalence of SOE ownership in China's capital markets, anecdotal and observed data on the prevalence of SOE ownership among LLCs and other ownership categories, and the SOE role in round-tripped FDI, it is reasonable to conclude that by 2009 nearly half of China's economic output could be attributable to either SOEs, SHEs, and other types of enterprises controlled by the SOEs indirectly. If the output of urban collective enterprises and the government-run proportion of TVEs are considered, the broadly defined state sector likely surpasses 50 percent.' (Andrew Szamosszegi & Cole Kyle, 2011, p. 25)

SOEs account for 28% of formal urban employment identified by the NBS for 2010; this means that informal employment of migrant workers is excluded (the incorporation of unregistered migrant workers is a primary concern of government policy today, this subject is dealt with extensively in the chapter of this thesis about the working class in China). The data also excludes SHEs as well as other mixed enterprises where SOEs are controlling shareholders which, if included, would significantly increase the role of the state in employment.²¹

Thus, according to the NBS figures on total urban employment for 2015, the categories that Huang defined as state owned or controlled sectors employed 149 million urban workers. That is over 40% of the urban workforce: This is broken down as follows:

State owned units 62 million 17 percent,
Collectives 4.8 million 1%
Coops 920,000 0.2%
Limited Liability companies 63.8 million 17%
Share Holding Companies 17 million 4%. ²²

3.7.2. Investment and the commanding heights

Kornai identified investment hunger and forced growth as system specific attributes of socialist political economy. They are driven by the perceived need to rapidly overcome economic backwardness and catch up with the advanced capitalist countries. All levels of the bureaucratic apparatus

promote rapid expansion to increase their sphere of power. Whereas the rapid development of capitalist firms is restrained by personal risk, under socialism, this constraint does not exist. Socialist investment hunger is only constrained by fear of sanctions for making mistakes and restrictions on resource allocation (Kornai, 2007, pp. 160–163).

The Ministry of Finance (MOF) was responsible for the collection and allocation of all financial surpluses prior to 1979. The People's Bank of China (PBC) was its sole bank. SOEs' budgets were part of the state budget and the PBC was the accountant and cashier of SOEs. SOE reforms led to the restoration of four state-owned commercial banks. Reform permitted bank lending related to increasing deposits, and the stock exchanges in Shanghai and Shenzhen became sources of direct finance for listed companies and banks. Now state enterprises use profit retention, stock markets, banks and financial intermediaries (e.g. state owned insurance companies, investment companies and leasing companies) as sources of finance for state enterprises. The government restricts financial markets through controls over entry into the banking sector, restrictions on stock exchange listing, and by interest rates (Lin, 2012, pp. 185–186).

Fixed investment may be the most appropriate means for determining the influence of the state sector because it reveals the forces determining the direction and orientation of the economy (Huang, 2008, pp. 20–22). This view is reinforced by data on the share of state investment in a variety of sectors.

Given the fact that SOEs are 'not completely market based, liberalising the financial market would have greatly increased their capital costs' (Lin, 2012, p. 208). The Chinese financial system is treated as an instrument of state policy. Stock exchange listing is too costly for small and medium sized private sector companies,²³ and SOEs receive 80% of bank loans. Therefore the development of the private sector is 'crippled due to the lack of a normal financing channel' (Lin, 2012, p. 209).

‘In the majority of industries, the SOE/SHE (State Holding Enterprise) share exceeds 50 percent, as does the median share.’ (Andrew Szamosszegi & Cole Kyle, 2011, p. 15). ‘SOEs and SHEs account for the majority of investments in most major sectors of the Chinese economy.’ (Andrew Szamosszegi & Cole Kyle, 2011, p. 16)

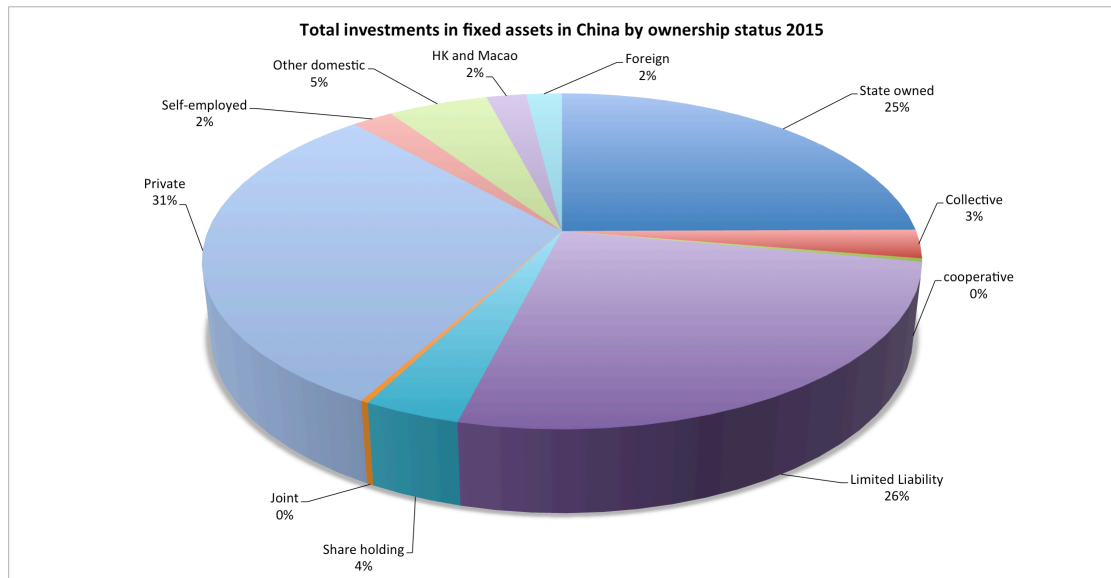


Figure 5. Chart showing investments in fixed assets by ownership status

The above chart records the percentage of total investments in fixed assets in China in 2015 by ownership registration. The data comes from the National Statistical Yearbook 2016.²⁴

The segments on the right of the chart are composed overwhelmingly of state owned or controlled entities. As limited liability companies, shareholding companies, collective and cooperative firms are all dominated by public sector ownership or control.

However, shareholding companies and limited liability companies are often categorized as capitalist enterprises. Many do indeed have significant private equity stakes, but many, if not most of these nominally private entities, are either majority owned by state entities, or have very significant state or state institutional ownership stakes. Such mixed ownership companies expanded rapidly from 2001, and by 2008, they

held 'half of the country's total capital assets and generated over 35% of the national total sales income' (Lin and Hu, 2011, p. 728). However, even though they are formally more independent than SOEs they are still made to serve party-state planning objectives.

The specific nature of China's hierarchy of authority - deriving from the combination of Communist Party rule of the state and public ownership of the commanding heights of the economy - concentrates and multiplies the power and control over all the non-state sectors of the economy and wider society. This power multiplier stems from the totality of instruments at the disposal of the party. The leadership of the banks, judiciary, education, police, secret police, army, mass media, government officials, trade unions, youth organisations, national minorities and religious groups etc. are all vetted and selected by the Communist Party. Thus, deemphasising the issue of whether the majority of GDP derives from the state or the non-state sector or whether the majority of workers work for the state sector - as the definitional determinant of the system –is entirely consistent with the method used by Kornai to define power relations in his socialist system.

Kornai questioned the viability of attempts to rationally combine bureaucratic and market coordination, as one of the system specific features of reform socialism is that horizontal coordination remains subordinate to indirect vertical dependence. Although 'manager's dress, vocabulary, and demeanour begin to resemble those of his or her Western counterpart', these managers lack the identification with the profit motive characteristic of capitalist owners. Their positions are dependent on evaluation by their superiors in the bureaucratic administrative hierarchy (Kornai, 2007, pp. 504–505).

In corporations predominantly owned by central or local government or by state entities, the leading executives are appointed by party and government agencies. They are actually civil servants, whose roles rotate between public industry and government positions. Managerial ownership stakes remain insignificant and managerial remuneration is

modest. 'Almost all of China's largest and most powerful corporations are still in this category.' (Walder, 2011b, p. 31)

The *Financial Times* reports on the impact of new rules to control the earnings of senior SOE managers: 'Wang Yilin, chairman of China's largest energy group CNPC, has been earning just \$107,000 a year — equal to what ExxonMobil boss Rex Tillerson, Donald Trump's nominee for secretary of state, earns in less than a day and a half.' ²⁵

3.7.3. Relations to the private sector

Kornai's description of the development of the private sector in reform socialism involves the spontaneous emergence of private enterprises when the hostile environment of classical socialism is reduced or eliminated. Part of the bureaucracy supports the private sector because it improves supplies and eases shortages and can reduce social tensions (Kornai, 2007, pp. 431–435).

However, another part of the bureaucracy relates to the private sector in an obstructive fashion and sometimes the attitude of bureaucrats changes from supportive to obstructive. The bureaucracy governs the public sector from within, and the private sector from without. Private sector autonomy is difficult for the bureaucracy to stomach. Such resistance to private enterprise is a spontaneous and natural reaction of the bureaucracy in defence of its power and ideology (Kornai, 2007, p. 450).

The bureaucracy fails to adequately guarantee the security of private property and controls access to all manner of permits and licenses. Restrictions can be placed on the size of firms and the sectors that are open to the private sector. The legal infrastructure is not designed to serve the enforcement of private contracts and leaves few avenues of redress against the state itself. Taxation can be arbitrary, and bureaucratic control over access to credit, materials, and state

procurement orders, acts as a severe constraint on private sector development (Kornai, 2007, pp. 451–454).

In academic and policy debates on the speed of systemic transformation during the 1990s, Kornai maintained that the transition should be organic, in the sense of not being excessively disruptive (Kornai 2008:79), and he argued that the design and implementation of comprehensive reform, requires experimentation and institutional transformation, whilst maintaining a broad constituency of support. Thus, ideally, such changes would impose a minimal negative impact on living standards (Kornai 2008: 80, 160-1).

Kornai argues that an organic and gradual economic transformation from socialism to capitalism has been completed in China. The process was characterized by an evolutionary development towards private sector domination, stemming from the dynamic nature of entrepreneurial drives, which, encircled and outperformed the state sector. The main spheres of economic activity of private sector enterprises described by Kornai in 1992, were small scale, although some medium and large private enterprises also existed at that time.

In the ideological sphere the growth of private enterprise provokes a crisis under reform socialism, in which pragmatism clashes with socialistic and anti-capitalist tendencies, provoking deep-seated reactions from broad sections of the population and within the ruling party (Kornai, 2007, pp. 444–447).

In China private ownership restrictions were first relaxed in 1982. At the 15th Party Congress in 1997, the private sector was declared to be an 'important component of China's socialist market'. The proposals were the subject of negotiation and sharp conflict, which reached a peak in 2005, when Gong Xiantian, a professor at Beijing University, publicly criticized the law in an open letter. This gathered support from thousands of prominent figures, including scholars, retired officials, and military generals - all opposed to a watering down of socialist property law. A

furious public debate caused the legislative process to be temporarily suspended and further amendments were incorporated to deflect leftist concerns (Lee, 2010, pp. 37–40). In 2004, a constitutional amendment recognized private property, and in October 2007, the Real Property Rights Law was finally passed. The long and complex process behind the passing of the 2007 law, probably reveals that the CCP, the government, the state, and wide layers of the general public, retain an ambivalent and conflicting relationship to the fundamental underpinnings of capitalist property relations (Lee, 2010).

The pressures to introduce legal protection for private property came from various sources. Foreign investors and states sought guarantees for the security of their investments. Domestic private enterprises developed into a significant part of the national economy, and their owners could be more readily co-opted in a legal environment that was friendly to private property. The Marxist ideological framework, within which the state operates, required some form of adjustment that would strike a balance between stability and legitimacy (Lee, 2010, pp. 29–31).

The private sector in China developed in an environment that was often hostile towards it, and access to critical inputs remains restricted by the in-built bias towards SOEs, and by the exclusion of the private sector from access to resources allocated by plan. Indeed, private sector firms often live in fear of expropriation. However, discrimination against the private sector by local government is more pronounced in those areas where SOEs predominate in the local economy. An IMF study found that private enterprises were 90% self-financed, and a Chinese Academy of Social Studies survey in 2003, found that fees extracted by local government, consumed 70% of private enterprise profits, and this did not take account of the cost of approvals, permits and associated ‘red-tape’ (Kung, 2011).

Huang provided strong empirical evidence to contradict the gradualist and evolutionary interpretation of the development of Chinese capitalism. He located China’s dynamic entrepreneurialism within the largely private

rural Township and Village Enterprises (TVEs), formed by peasants in the 1980s. Thus, TVEs - originally the foundation for rural capitalism in the 1980s - were forced back under government control by the repression of rural finance to private sector TVEs. This entailed a return to promoting cooperative firms with private revenue rights, which functioned under effective government control (Huang, 2008).

However, he shows that private and state funding of private enterprises was repressed and a general policy bias towards urban state-owned and controlled sectors prevailed. In the 1990s rural capitalism was repressed and village level democratic control was transferred to higher levels of power, i.e., to expanding, unelected, bureaucratic organizations at the township level. In the 1990s, private companies were starved of finance, and larger-scale collectivist TVEs, under the dominance and control of local government, were backed with finance, and by policy initiatives that produced paper viability (Huang, 2008, pp. 133–174). Such entities operate under soft-budget constraints.

3.7.4. CCP ideology and the commanding heights

The standard view of capitalist progress in China is that the CCP leadership encouraged market incentives but were overwhelmed by the capitalist genie they unleashed. And, thereafter, they mainly reacted to market driven imperatives, rather than consciously steering events. However, Sarah Eaton studied the CCP's official discussions and shows that they pursued policies that were designed to guarantee the primacy of state enterprises from the late 1980s onwards. She discovers a consistency and continuity in the ideological justifications used to defend the policies pursued. She examines how the emergence of state-owned empires was structured around enterprises in those sectors designated as the commanding heights. Although a vocal pro-market lobby exists, which decries the monopolistic power of SOEs, policy-makers defend their monopolistic power. Indeed the CCP leadership see state monopoly as a means to defend state enterprises against more powerful international players (Eaton, 2014, p. 14).

The vertical hierarchical structure of SOEs from Mao's day was replaced by large-scale horizontal relations, which integrate and unify enterprises within interlinked sectors. The increased scale improved the focus of capital intensity. So, in the 1990s the state encouraged the formation of large state enterprise groups with monopolistic power. Consequently, Chinese economic theory and practice diverged from the neoliberal trend led by Britain and the United States. When China joined the World Trade Organisation and signed up to its free market rules; state enterprises leading the 'national team' were considered to be the last line of national economic defence, as well as the mechanism for reaching outwards through international joint ventures, alliances, and corporate acquisitions.

Internal documents informing senior Chinese official debate reasoned that the most successful capitalist enterprises and nations flourished due to the extinction of free competition and the victory of monopoly capitalism. Interest in Japanese developmental policies identified large-scale socialized production groups as the core of Japan's success (Eaton, 2014, p. 10). Despite the policy of encouraging markets, planning was reformulated to rely on large enterprise groups in the commanding heights. State companies used public listing as a means of raising capital - without ceding control or ownership. And they sought to improve efficiency and enforce the government's regulatory role over the economy.

In the 80s and 90s, the senior level internal party debates on SOE monopoly power, were a contested ideological terrain. This remains true today. Eaton notes that a Marxist analysis of the concentration of capital and the tendency towards monopoly was used to justify the inevitable concentration of capital in a commodity economy. Competition - between and within large enterprise groups - can be said to constrain and ameliorate monopolistic distortions. However, bureaucratic decisions and interests - rather than profits - often lay behind enterprise marriages. Some reports to officials advocated the eradication of this 'rigged' market that unifies the power of large monopoly enterprises and government. In

particular China's 'New Right' economists like Zhang Weiying continue to denounce this (Eaton, 2014, pp. 16–18). Eaton finds historical continuity evident in the 'advance of the state' thesis that has been central to Chinese government and intellectual debate since 2008. However, neoliberal thinkers and pro-market publications maintain that interests bound to the state sector are holding back political and socio-economic transformation.

Sarah Eaton's assessment was confirmed by President Xi Jinping's, 2016 speech to a National Conference on Party Development in SOEs, where he said that the objective of Party activity in SOEs is to 'make them the most reliable force of the Party and country and a major force in implementing the decisions and plans of the CCP Central Committee [...] We should implement policies that preserve and increase the value of state assets, and make consistent efforts to help SOEs become bigger, stronger and better.'

'SOEs serve as a material and political foundation of socialism with Chinese characteristics.' (Xi, 2017, p. 192)

And he insisted that Party organizations must continue to decide on the appointment of SOEs leaders, and even though the Party appoints business leaders to manage state assets this trust must be subject to strict and all encompassing supervision from the party and the workforce (Xi, 2017, pp. 193–194).

3.8. Planning in contemporary China

Since 1953, China's planning system operates through five-year plans. Originally, the plan directed state owned companies in production decisions, and government ministries were responsible for each sector of the economy. After 1978, when non-state competition was permitted, planning was subsumed under the ambit of 'reform' and 'development' leading to the creation of the National Development and Reform Commission (NDRC) in 2006. The Central Committee of the Communist

Party drafts Five Year Plans (FYP), which are amended and adjusted under the control of the NDRC before approval by the National People's Congress (Chow, 2011, pp. 1–2).

The various bureaucratic entities that were combined to form the NDRC are steeped in a culture, habit and outlook that allot the primary role to planning and a supplementary role to markets. The NDRC is composed of an amalgam of bureaucratic administrative organs directly inherited from the history of central planning. They set the targets, and the State Council, through its ministries and offices, is tasked with implementing them (Chow, 2011, pp. 5–6).

The direct control of the economic resources of state-owned enterprises is the primary means by which the plan is realised. In addition, monetary and financial policies encourage non-state entities to help achieve planning targets using interest rates, subsidies, tax breaks, government procurement, and contracting policies. Party secretaries at all levels of society are directed to ensure the Plan is realized, and government agencies at all levels must implement the Plan under the direction of Party organs (Chow, 2011, p. 7).

Kornai identified a distinct tendency within socialism that seeks to amend, adjust and perfect mechanisms of bureaucratic coordination, whilst leaving one party rule and the dominance of public property intact. This involves reshaping organisational control by function or location, or by means of centralisation and decentralisation. Public firms are reorganized into ever-larger units and computer models are devised to improve control systems (Kornai, 2007, pp. 396–408). Kornai believes that the complexity of millions of transactions in a national economy make calculations to effectively regulate and plan impossible. And he argues that only the free market can carry out these functions, which it does automatically. This is a contention that one might question in today's networked economy, and that has previously been challenged on non-technological grounds²⁶ (Lange et al., 1938). Indeed, some Chinese scholars are questioning how the advent of big data affects the capacity

to plan an economy effectively in ways that can supplant the markets (Wang and Li, 2017). However, here we are not seeking to establish the validity or error of his claim, but to identify the degree to which Kornai's description of reform socialism fits contemporary China.

According to Kornai, those seeking to perfect the system, seek a reduction in the quantity of planning indicators, and place greater emphasis on a smaller number of objectives. They concentrate on quality not quantity, separate targets from past performance, and concentrate on net production. However, the self-interest of decentralized bureaucratic entities comes into conflict with the central bureaucracy. To eliminate this 'imperfection' the central bureaucratic apparatus reasserts its authority and control. It tightens discipline and centralizes coordination and command. The identification of corporate 'profits' as the primary target indicator produces the superficial impression of a radical shift towards capitalism. However, Kornai believes that without decentralisation, free entry and free competition, profits cannot be used as the defining characteristic of capitalism (Kornai, 2007, p. 406).

Research by Heilmann and Melton (2013) on the revitalisation of state planning reopened a closed debate in western scholarship. It challenged the consensus represented by Naughton (1996), who argued that the market had conquered China in 1993, after being given the green light by Deng Xiaoping in 1992. According to this theory, planning had faded into insignificance, and any enduring influence is the shadow of a once ubiquitous system. Naughton responded to Heilmann and Melton's challenge by accepting that the 'planning process is deeply integrated with other aspects of the Chinese political system, especially the policy-making and implementation process, and the cadre evaluation system' (Naughton, 2013, p. 642).

His dispute with their theory on the revival of planning centres on the definition of planning. A default reversion to resource allocation based planning in which the 'market economy coexists with numerous distortions, underdeveloped institutions, and actors who have incentives

to invest in projects with zero returns' is decried by Naughton (2013, p. 647) as in his view planning 'necessarily involves influencing behaviours to become consistent with a politically generated set of objectives' (Naughton, 2013, p. 648).

He says that after 1993 resource allocation planning gave way to systems transformation and institution building to help marketization. However, although the state budgetary situation improved from the late 1990s onwards, rather than carry through promises made at the Third Plenum in 2003 - to complete the change to a market economy - Premier Wen Jiabao spent increasing government revenue on vast and ambitious government investments. Naughton complains that this process escalated with the onset of the 2008 world economic crisis, 'the shift towards more planning after 2003 has *not* been accompanied by adequate further movement towards a well-functioning market economy' (Naughton, 2013, p. 650). Instead, Naughton believes, marketization was put on ice.

The sabotage of the reform agenda agreed at the Third Plenum in 2013 was the consequence of a coalition of the four of the most powerful state bureaucracies that was formed around 2009. According to Shambaugh (2016) the Party propaganda apparatus, the Ministries of State and Public Security, the state owned enterprises, and the People's Liberation Army and the People's Armed Police undermined political reforms which they feared would spin out of control and ramped up the security apparatus instead. The post 2008 world economic crisis reinforced a sense of moral and economic superiority amongst the Chinese leadership. The ascendance of Xi Jinping and his anti-corruption campaign has been accompanied by a more and more illiberal atmosphere and by the reintroduction of many forgotten symbolic policies, rituals and forms of language. For example, Xi's appeals to the popular masses through promoting simple living puts pressure on cadres to experience the lives of the people, and the anti-corruption campaign has spread fear amongst those engaged in corrupt practices. This has been promoted by the massively popular TV show called In the Name of

the People, which delves into multiple forms of corruption, presents the subtle nuances of the consequences of graft within wider society, and shows how trustworthy and honest Party member and cadres intervene to resolve outbreaks of social unrest. And a young and determined anti-corruption team is pursues corrupt cadres with determination and zeal.

For Naughton, present-day planning retains basic market hostile mechanisms and instruments. He cites the way the National Development and Reform Commission (NDRC) intervenes in macro-economic policy, in a way that produces excess liquidity and asset bubbles. It is unclear why Naughton considers excess liquidity and asset bubbles in China to be illustrations of hostility to markets; after all, asset bubble and liquidity problems are common features in mature market economies. What is unusual is the way China contains the negative impact of market crises.

Heilmann and Melton's (2013) comprehensive study of China's planning system covers the period 1993-2012. They explain that the plan has 'provided room for market forces' and simultaneously enhanced the 'state bureaucracy's ability to influence the economy' and maintain party control. Planning remains 'central to almost all domains of public policy making and the political institutions that have fostered China's high speed growth and economic stability' (Heilmann and Melton, 2013, p. 581).

Under Wen Jiabao, planning, fiscal, and monetary policy would become the three mechanisms of macro-economic control. Planning would concentrate on strategic issues and policies, and allow flexibility to the institutions responsible for implementation. In the Tenth Five Year Plan (2001-5) proportionality and the balancing of supply and demand became central objectives. Imperative targets were abolished and resource allocation was to be market dominated. Planning would focus on qualitative targets, and coordinate the urbanisation process and the development of the interior and west of China. It would also target scientific, technical, environmental, and human resource issues. In order

to overcome various imbalances in development; social welfare, administrative competence and public services, became the focus of the 11th Five Year Plan (2006-2010). The plan was now composed of binding targets, anticipatory, and indicative targets. Binding targets are set for government bodies and refer to various promises particularly in public service provision. This established 'a direct link between China's top policy priorities and the party's control over the leaders of major institutions and state-owned enterprises, the plan-cadre nexus' (Heilmann and Melton, 2013, p. 586).

This plan-cadre nexus welds the action of cadres through its discipline and reward structure to the priorities set in state planning objectives. So the incentives to meet planning targets are integrated with the career structures of the party. The Central Committee draws up initial guidelines which are converted into thousands of sub-plans to be implemented by government entities at all levels of administration. In addition to the overall Five Year Plans there are three core sub-plans, comprehensive, macro-regional, and special plans. The initial approval of plans begins an unceasing process of coordination and evaluation that draws together the operations of bureaucratic agencies (Heilmann and Melton, 2013, pp. 586–590).

Kornai noted that boom-bust economic cycles under socialism are aligned with the calendar pulsation of the planning system, with speed-ups clustered at the end of annual plans. The Chinese planning system since 1978 has certainly experienced a far smoother growth pattern than classical socialist systems based on ubiquitous public property and planning. However, Heilmann and Melton point to a similar and related phenomenon in the Chinese planning cycle: 'the regular five year planning periods are not synchronized with the turnover in party and state leadership. Incoming leaders remain bound to the previous plan for three full years and thus cannot openly discard the policy goals set down by their predecessors [...] The "CCP rhythm," not the rhythm of State Council turnovers, thus governs plan making.' (Heilmann and Melton, 2013, p. 608)

3.8.1. The 12th Five-Year Plan (2011-2015)

In the 12th Five Year Plan, the SASAC identified key sectors for supportive government intervention including strategic and emerging industries. This entailed the assimilation of imported know-how and its transformation into emulation and innovation. This policy was consolidated through state sector investment regardless of whether took place at the expense of private sector competitors. Competitive capacity in global terms was facilitated by preferential state support through such methods as credit policy, tax preference, and state procurement policies (Andrew Szamosszegi & Cole Kyle, 2011, p. 2).

Hu says that the 12th Five Year Plan involved several stages, which included evaluation, research, suggestions, conceptualisation, consultation, review, brainstorming, deliberation and approval. He says that this approach draws on democratic centralist methods where the contrasting views of interested parties are aired and debated and the decisions reached are implemented. Hu notes an increasing correspondence between local and national objectives and indicators, and he claims 'the performance of governance is far higher not only than in the period of the planned economy, but also higher than in the mature market economy of Western countries [...and] is an important source of the miracle of the Chinese economy' (Hu, 2013, p. 637).

Industrial policy contained in the 12th FYP supported 'Strategic Emerging Industries', biotechnology, new energy, high-end equipment manufacturing, energy conservation and environmental protection, clean-energy vehicles, new materials, and next generation IT. The 12th FYP envisaged expanding these industries from between 2-4% of GDP in 2010, to 8% by 2015, and 15% by 2020. Naughton said that if this is realized 'they will be large industries driving the whole development process' (Naughton, 2011, p. 325).

The 12th Five Year Plan (2011-2015) affected nearly every aspect of society: agriculture, industrial upgrading, service sector expansion,

regional and urban development, energy and environment, education, science and technology, people's livelihood and welfare, the management of society, promoting socialist culture, perfecting reform, advancing the open door policy, promoting democracy and socialism, establishing a harmonious society and strengthening defence. The FYP document outlines guiding concepts and directions and the means of executing them (Chow, 2011, pp. 2–3).

The objectives of the 12th FYP are defined through numerical targets. These included the following categories: total GDP and per capita GDP; the increase in the service sector as a percentage of output and employment; expenditure on research as a percentage of GDP; the rate of urbanisation; total population; reducing energy usage and carbon emissions; the quantity of cultivated land; years of schooling; the extent of urban employment and unemployment, insurance and disposable income; rural health coverage and net income. The objectives are designed to rally support behind the realisation of these targets (Chow, 2011, pp. 3–5).

The Five Year Plan Process

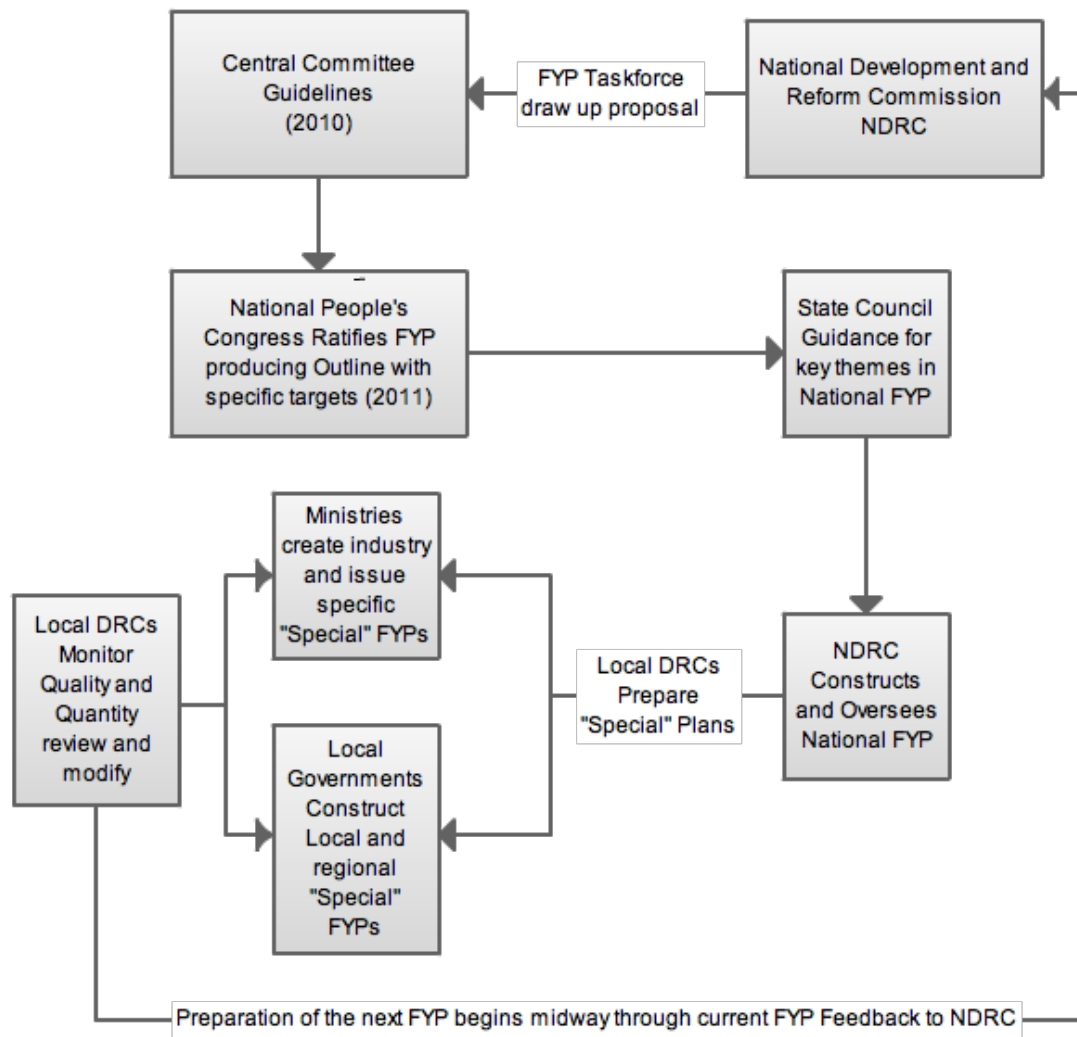


Figure 6. Chart of China's Five Year Plan process

Its targets for social policy were overwhelmingly state driven policies aimed at expanding public sector control over housing, healthcare and education. Compulsory 'binding targets' to be attained by 2015 in these sectors included:

1. An increase of urban residents enrolled in the basic pension scheme from 257million to 357 million
2. Building 36 million apartments for low cost rental to low-income groups.

3. Basic urban and rural medical insurance enrollment is to increase by 60 million. The percentage of state payment is to exceed 70 percent Binding targets for environmental protection included:

1. A 16 percent reduction in energy consumption per unit of GDP
2. A 17 percent reduction in CO₂ emissions per percentage of GDP

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According to the report by the National Reform and Development Commission delivered to the Twelfth National People's Congress on 5 March 2016 nearly all of the 12th FYP targets were met. Of the 59 main targets contained in the FYP, the results for 5 targets fell below expectation: natural gas production, the total import and export volume, spending on R&D as a percentage of GDP, total fixed asset investment and total retail sales of consumer goods. All the other 54 FYP targets were met. This includes all GDP targets, 6 out of 7 targets for the output of industrial and agricultural products. All 4 out of 5 external trade and investment targets were met. The inflation target was met, as were the targets for government revenue, expenditure, deficit and the money supply. All the social, population, urbanization, health and clean water targets were met, as were those concerned with education and the environment.²⁸

China now stands uniquely alone amongst developing countries in Naughton's opinion because it carried through a significant shift away from the market and towards state interventionism following the world financial crisis of 2008-9 (Naughton, 2011, p. 328).

The experience during the 12th FYP closely resembles Kornai's description of attempts to perfect a system of planning under reform socialism (Kornai, 2007 see chapter 13). The CCP claims it is pursuing 'scientific development' and seeks to promote a government led 'informationization' strategy. Hu Angang identifies a shift from planning economic growth and structural changes to planning non-economic issues concerned with education, science, technology, environment, resources and people's livelihoods. He describes this as a shift from economic planning to public affairs governance. In his view, markets and

planning constitute invisible and visible hands, the planning system is visible to market players and so is considered helpful. This process of planning is described by Hu as 'democratized, scientized and institutionalized' (Hu, 2013, p. 633).

3.8.2. The new urbanization plan

During the reform era, registered urban residents experienced spectacular improvements to their housing conditions. Meanwhile migrant workers tended to live either inside their workplace or in squalid 'urban villages' on the outskirts of cities. However, the Party's planned urbanisation drive encompasses the staggered, but extremely rapid, integration of peasant-workers into the urban system. The provision of housing, social and welfare services to migrant workers and their families is central to this. It is designed to consolidate a vast new constituency of social support for the party. Zhang Xueqin, the vice director of a bureau for public housing under the Ministry of Housing and Urban-rural Development claimed that nearly 100 million people benefitted by 2011. With public housing offered to 26.5 million households in 2011 and 4.5 million households financially supported. Although it is said that housing for workers of state enterprises and other types of companies made up half of the low cost housing built that year.²⁹ In the period 2011-13 work began on building 24.9 million subsidized housing units, of which, 15.8 million were completed (Oecd, 2015, p. 126). The NDRC 2016 report claims that 28.6 million units of urban government- subsidized housing had been 'basically completed' and 40.13 million had been started. In addition 19.94 million dilapidated rural homes had been renovated.³⁰

It is incontestable that China's per capita urban housing space (for urban residents) has risen dramatically year on year. In the 1970s average per capita urban living space was just 3.6 m² (Lui cited in Yang and Chen, 2014, p. 2). This rose to 13.7 m² in 1990 (Yang and Chen, 2014, p. 22) and 30m² in 2009 (Yang and Chen, 2014, p. 24). Improving the housing provision for newly designated urban residents is a powerful tool to win support for the CCP.

Land in urban China is owned by the state, and rural land is collectively owned.³¹ Land usage rights may be leased for profit in designated urban areas, but the same practice is illegal for rural leases from village collectives. The control of land is a major source of contemporary capital accumulation, both by state entities and by private individuals and companies. Urbanisation has led to battles between contending users and claimants to land usage rights. Forced evictions and conflicts about land seizures are common sources of urban and rural unrest. Local state planners, landlords, financiers, builders, and an ever-expanding urban state apparatus drive the process of urbanisation. Local leaders seeking land rents as revenue sell real estate projects in which rising property prices are used as indicators of success (Hsing, 2010, pp. 6–10).

The conflicting claimants to the control rights over land usage are territorially divided; this generates three primary levels of intra-state land disputes. 1. Between municipal governments and state entities such as SOEs, universities, the military etc. in the major cities. 2. Between urban and rural governments at the fringe of the expanding cities. 3. Between township and village governments at the rural fringe (Hsing, 2010; Huang, 2008, p. 15). Huang believes that land grabbing may fundamentally undermine the faith of rural entrepreneurs in the security of property rights. On the one side, land grabbing is certainly a lucrative means for bureaucrats to transfer public resources to private hands through corrupt property deals. On the other, it also involves state bureaucracies extending the wealth, power and reach of the urban state. To a significant degree this conflict determines who owns China.

China's urbanization plan seeks to shift economic geography to develop the interior by means of massive investment in infrastructure. Regional plans are granted significant experimental autonomy but are often centrally coordinated. Regional governments make implicit contracts with the central government to meet development objectives. The use of experimentation and competition in policy implementation is a common feature of China's reform era. National special plans concentrate on

large-scale investments in infrastructure and the use of key resources, as well as the provision of core public goods and services. These plans are developed during the Five Year Plan period and include industry specific plans. The drawing up of plans involves multi-level and multi-agency consultation and the elaboration of targets and financing on an on-going basis (Heilmann and Melton, 2013).

China's urbanisation plans were tested in Chongqing in advance of the national roll out. A massive expansion in the public sector provision of housing, which emulated the Chongqing example was adopted as a national model in 2010 and then integrated into the 12th Five Year Plan in 2011. China's New Urbanization Plan 2014-2020 seeks to integrate 300 million people into urban life. According to the plan, 100 million migrants who already live in urban areas are to be granted urban residence by 2020. This allows them to gain access to the full range of welfare and social rights. A further 100 million who live in run-down urban areas are to have their accommodation renovated or rebuilt, and 100 million rural residents are to move to the cities in central and western regions of the country. This plan, launched in 2014, and to be realized by 2020, comes in for criticism from Hu and Chen (2015) because it is 'heavily affected by the planned economy and it is essentially plan-led urbanisation' (Hu and Chen, 2015, p. 39). The projected cost of this New Urbanization Plan is estimated to be RMB 42 trillion (US \$6.8 trillion) according to China's Ministry of Finance.³² It should be noted that this Plan was not part of the 12th Five Year Plan, yet top-level endorsement ensures that truly colossal resources are being mobilized to realize it.

Philip Huang (2011) suggests that the economic and political policies pursued in the Chongqing municipality under the leadership of its ousted former mayor Bo Xilai were a unique experiment. It combined market capitalism and planned socialism in a reconfigured way, which Huang claims, invalidates Kornai's theory, that an economy responsive to market signals requires that private firms be the mainstay.

Chongqing's government accumulated resources in public hands to finance social policy objectives and infrastructure projects. Its urbanization programme was a trailblazing experiment in the structured process of reforming the *hukou* and formalizing the status of migrant workers. The government courted large multinationals including Foxconn, BASF, Ford and Hewlett Packard to invest in Chongqing. This involved expediting delivery to seaports and creating an ambitious logistical infrastructure, which included building a new inter-continental freight railroad to Europe. The government provided resources such as land at a discount and the infrastructure to encourage investment in priority sectors by key enterprises called 'dragon-heads'. Eight state-owned asset management companies were charged with realising large-scale development in urbanization, transport, energy, water and real estate. Financing was raised on land assets, and the realisation of these projects further increased the land value. The use of land appreciation for public benefit is central to the Chongqing model. It was secured by infrastructural investment to facilitate urbanization and complemented by foreign investment and relatively low wages.

Chongqing's land exchanges offered peasants big incentives to trade unused land for about 100,000 yuan in cash when their residency status was urbanized, and they also offered significant subsidies and loans to open businesses in the city (Huang, 2011, pp. 596–598). In 2009 the Chongqing government spent over 68 billion yuan, more than half of its spending on improving 'peoples' livelihoods' (Huang, 2011, p. 589). Central to this social investment is the process of formalisation of migrant peasant-workers within the urban environment, the municipality recently built public sector rental housing for 2-3 million migrant workers and extended urban residency status to them. Chongqing aimed to provide low cost rental housing for 30% of the urban population, when many cities aimed at less than 5%. Chongqing aims to extend urban status to 10 million migrant workers by 2020 (Huang, 2011, pp. 591–595).

Alongside Bo Xilai's socio-economic programme in Chongqing, he initiated a campaign against crime, which focused on tackling organized

crime and its connection to money and power. The campaign became renowned for taking on corrupt senior local police and judicial figures, and for its depth, speed and severity. It solicited 40,000 reports and accusations from the public, 80% of which were signed, indicating confidence that they would not be persecuted for these submissions (Huang, 2011, pp. 602–604). Such popular engagement was reinforced by measures that forced officials to experience the living conditions in villages and peasant households. This is reminiscent of Maoist anti-bureaucratic campaigns and was accompanied by the promotion of leftist propaganda and nostalgia.

In 2012 Bo Xilai was removed from office, and in 2013 he was jailed for abuse of power, bribery and corruption. However, when Xi Jinping became the General Secretary of the CCP, he promoted similar socio-economic policies, which had already been integrated into the 12th Five Year Plan, and he initiated a far-reaching anti-corruption campaign reminiscent of Bo Xilai's campaigns in Chongqing.

President Xi Jinping said: 'the essence of urbanization is to bring more people to settle in urban areas. We should encourage those rural households which are capable of maintaining a stable job and life in urban areas to relocate there. In this way, we can achieve a steady increase in the labour supply, reduce the pressure of rising labour costs, and expand consumption in real estate and other fields. This is also the fundamental solution to narrow the urban-rural gap, promote urban and rural integration and agricultural modernization.' (Xi, 2017, p. 265)

3.9. State advances the private sector retreats

If the dominant macro-economic regulator is accumulation to realize the state plan, then the ability to mobilize the necessary resources is central to its success or failure. And the identification of those sectors of the economy that constitute the commanding heights will change according to priorities set out in planning objectives. In the period since 2004, and more especially since the world economic crisis of 2008, the phrase

guojin mintui 国进民退 meaning 'the state advances the private sector retreats' became a popular complaint from private business circles and amongst advocates of free markets. This process of strengthening state enterprises involves activities that channel the operations of competing private sector companies, or squeeze them out of business.

Many of the methods used constitute de-facto nationalisation. The coal mining industry in Shanxi is an example: private mines in the province have been highly profitable but have poor safety records. A number of mine disasters focused national attention on lax safety supervision and on the corruption of officials who turn a blind eye. In 2008 a mining accident killed 270 people and the governor of Shanxi province resigned. He was replaced by Wang Jun who ordered the wholesale consolidation of the province's mining industry. Only those mines with an annual output above 300,000 tonnes were permitted to continue operating and smaller mines would either fall under the control of state giants or be closed down.³³

When China's \$588 billion economic stimulus was launched in 2008 to counter the impact of the world economic crisis. State enterprises rapidly expanded the range and scale of their operations and intensified their vertical integration. Local governments established 8000 state investment companies in 2009 to manage these cash injections. State enterprises were able to access these funds to acquire assets and realize projects that their own profits and bank balance could not justify, for example, Zhejiang Geely Holdings acquired Volvo with money from such local government funds.³⁴

Another example is the airline industry, three state carriers, China Airlines, China Southern and China Eastern, dominate the passenger airlines industry. The government permitted private airlines to operate in 2004, and eight private airlines had entered the market by 2006, but they were soon squeezed out by various methods: state airlines refused to allow private companies to use the reservation system; they charged

private carriers higher rates for jet fuel; and they engaged in a price war. In 2010, only one private airline, Spring Airlines remained.³⁵

The process of state entry into the dairy industry was initially provoked by a food safety scandal about melamine-contaminated milk products. The state owned Yili Group established dairy cooperatives in which farmers are given shares to standardize the feeding, housing and milking of cows. This also offers efficiency and costs savings, and similar cooperatives are being promoted by large-scale investments. China's four biggest dairy companies are now all controlled by dominant state shareholding.³⁶

China's largest private steel company was Rizhao Iron and Steel, in the early 2000s it had successfully encroached on state dominated markets. But the state-owned Shandong Iron and Steel Group bought 67% of its shares in 2009 in order to consolidate the industry and expand total production.³⁷ A recent article in the *Financial Times* identified what it sees as counter-trend to the process of state advance, 'one Chinese province embraced privatisation to cast off its burden, setting a precedent for dealing with thousands of "zombie enterprises"' ³⁸ The state owned Dongbei Special Steel in Liaoning province allowed Shen Wenrong, a private steel tycoon with personal wealth of US \$3.7bn, to buy a 43% (a controlling stake) in the enterprise at a cost of RMB 4.5bn. Those who favour widespread privatization of SOEs cheered this decision. However, perhaps this actually represents the nationalization of Shen Wenrong's money and time? As the article explains an unnamed executive in Shen's company said, 'that the decision had "both commercial and political motives"'.

China's anticorruption campaign and President Xi's campaign to strengthen the Party's support and revive socialist idealism, 'can be interpreted as an acknowledgement that internal interest groups-rather than public interest-have been driving specific economic outcomes.' (Naughton, 2017, p. 21)

China certainly the means and intention to shape the nation's economic outcomes by plan. And 'even those who judge that the Chinese system today is not socialist might consider that the socialist ideal is still influential, and the system may continue to evolve in the direction of stronger "socialist" and redistributive institutions' (Naughton, 2017, p. 22).

3.10. Xi Jinping in power

After Xi Jinping became General Secretary and president in 2012, investment, through state owned industries, continued to dominate China's economy. Capital controls and low interest rates help to reproduce this model. Consequently, overcapacity and surplus production is ubiquitous and income inequality has reached extraordinary proportions.

In November 2013 the Third Plenum of the CCP's central committee announced a series of sweeping reforms, which included the pledge to upgrade the role of the market from 'basic' to 'decisive'. The market was supposed to determine prices in all instances where it could. Simplified regulations for foreign capital investment would be introduced and publicly owned enterprises would become mixed ownership entities, and even natural monopolies would lose their privileged access to resources. Executives would be paid market rates and asset management would give way to capital management. Banking reforms would facilitate access to loans by private companies, and interest rates were to be liberalized (Brødsgaard and Rutten, 2017, pp. 154–156).

However state owned enterprises were consolidated into larger monopoly organizations, acting as national champions in the world market in 2014, this was followed in 2016, by mergers in shipping, the power industry, and the steel industry. In October 2015 the central committee promoted 'supply-side reform' to eradicate excess capacity, excess costs for companies, excess housing stocks, and financial risks. It was designed to cut taxes and labour costs, reduce the real estate inventories of state entities and cut SOE debts.

As Brødsgaard and Rutten explain excess capacity in steel, coal, cement, chemicals, and other sectors is truly enormous. For example, in 2014 China's excess steel capacity was equal to the combined 'output of Japan, India, the USA and Russia.' (2017, p. 158) China's cement production makes up 57% of world production, between 2011 and 2013, China used more cement than the USA had throughout the 20th century (2017, p. 159). The downturn in global demand after 2008, exacerbated China's overcapacity problems, and accusations of Chinese dumping grew louder around the world.

Supply-side reform has been a top-down initiative, and encouraged provincial leaders to enforce this. 'However, in doing so they are confronted with powerful vested interests that feel hurt by production cuts.' (Brødsgaard and Rutten, 2017, p. 161) The pressure from angry workers in state enterprises commonly results in government intervention to meet their demands. So, despite announcements of large-scale layoffs in loss-making enterprises, to avoid social discontent political pressure has generally resulted in the reallocation of labour within these enterprise groups. This avoids creating unemployment.

China's 13th Five Year Plan 2016-2020 envisages growth rates of about 6.5% and a restructured economy; based on innovation, services, and increased consumption. Rising living standards should end poverty, and quality-of-life and environment should improve, and refining governance and public services provision takes high priority. However, colossal state investment programmes are set to continue. Indeed they have assumed a gigantesque scale. For example, the 'One Belt, One Road' initiative, involves the creation of land and maritime infrastructure linking Asia, Africa and Europe by road and rail (the Belt) and shipping lanes (the Road). If realized, this trade infrastructure will link up 60 countries, and more than half of the world's population. In theory, this could simultaneously provide an important outlet for the excess capacity of China's state owned giants (Brødsgaard and Rutten, 2017, pp. 162–164).

3.10.1 The anti-corruption campaign

President Xi Jinping's anti-corruption campaign targets 'flies' and 'tigers' the aim is to produce a climate whereby officials fear party disciplinary measures or court action more than they believe they can escape detection for corrupt practices (Xi, 2014, pp. 436–441). Xi invokes Maoist precepts concerning the relationship between the CCP and the people by reference to mass-line education, meaning that the party must maintain close ties with the people, and engage in criticism and self-criticism. He specifies four evils: formalism, bureaucratism, hedonism and extravagance; warning that the consequences of inaction against them would result in the downfall of CCP rule (Xi, 2014, pp. 401–405).

Anti-corruption campaigns escalated significantly after Xi was elected. There were 140,000 officials punished for disciplinary offences in 2011, 160,000 in 2012, and 180,000 in 2013 (Yuen, 2014, p. 42). Most of them were lower level officials punished by the party's Central Commission for Discipline Inspection (CCDI), which has powers of search, interception of communications, detention, interrogation, and seizure, backed by the police and courts, and it can forward charges to state prosecutors. Party disciplinary crimes include categories, which do not exist in the criminal code. Xi's anti-corruption campaign escalated between 2013 and 2017 when a further 1.34 million officials were punished.³⁹

Various manoeuvres were introduced to overcome the resistance of protective networks. Fu (2014) notes that a corresponding crackdown on attempts to organize independent campaigns against corruption excludes popular participation in the anti-corruption effort, except for those that are conducted online. This phenomenon is known as 'human flesh' searching. If, for example, an official wearing an expensive watch is photographed and posted online, people try to identify and expose them on the Internet. Often the authorities are compelled to take action, although defamation suits and the fear of being accused of illegal activism, tempers such online activity. However, the anti-corruption campaign has re-centralized and re-concentrated power in the hands of the party and its leader.

3.11. Conclusion

In this chapter I have contrasted Kornai's general method for classifying socialism with his specific statements on China. Kornai's analysis of reform socialism describes its inner workings and dynamics. He elaborates the idiosyncrasies, contradictions and incoherence that penetrate the system as reforms take root. Notwithstanding this, he recognized that some countries were able to sustain reform socialist combinations for decades before facing revolutionary change.

Kornai's reluctance to compare contemporary China to his own reform socialist theory is perplexing. Surely, such a method could help to identify which 'remnants' of China's reform socialist past continue to display vitality; and which are withering vines and empty shells, that will inevitably fade away as new capitalists sprouts bloom?

I believe that Kornai's writings on contemporary China have drawn premature conclusions about the extent of its systemic transformation towards capitalism. Indeed, there is a growing body of research on Chinese political economy that also questions the degree that China has 'transitioned'. When this research is dovetailed into Kornai's original model of reform socialism, it produces a very close match to this 'genetic code'. I find that all three of the basic criteria that Kornai uses to define reform socialism apply to China. China's system of political economy remains dominated by the party, the bureaucracy and public ownership. This conclusion reinforces the strength of Kornai's original theory but also poses new questions about the nature, longevity and potential of Chinese socialism and indeed of socialism in general.

There are also some key differences between Kornai's original concept of reform socialism and China today. There is a far greater role for the market and private ownership than in any previous socialist experiments. China has experienced a prolonged and exceptionally rapid rate of economic growth. This enabled the Communist Party to ameliorate many of the conflicts that undermined other socialist systems.

¹ In Yugoslavia 'the bulk of prices for products and services were freed at the earliest phase of the reform process and the area where administrative prices apply remained narrow.' (Kornai, 2007, p. 514)

² http://usa.chinadaily.com.cn/china/2014-07/01/content_17628308.htm (Accessed 16.35 GMT 25 Jan 2015)

³ It is not clear how this figure was arrived at. It appears to include any entity that is not specifically designated as a private entity (Lawrence and Martin, 2013, p. 20).

⁴ <http://www.globaltimes.cn/content/711238.shtml> (published 25 May 2012, Accessed 09.23 GMT 30 May 2015)

⁵ The 7-man Politburo Standing Committee (PSC) operates by consensus. The Politburo has 25 members and its 7-member Central Committee Secretariat coordinates the implementation of decisions. The full Politburo meets several times a year to deliberate on big issues or to prepare major events.

⁶ The PSC and the General Secretary determine the composition of the Central Military Commission. In 2012, the outgoing CC was composed of leaders from the provinces (41.2%), central ministries (22.6%), the military (17.5%), central party organizations (5.9%), and state owned enterprises, educational institutions, "mass organizations" such as the Communist Youth League and other constituencies (12.4%) (Lawrence and Martin, 2013, pp. 22–24).

⁷ http://english.chinamil.com.cn/news-channels/china-military-news/2014-11/03/content_6208959.htm (Accessed 15.01 29 January 2015)

⁸ The NPC is elected every 5 years and meets approximately 10 days a year. Its Standing Committee undertakes its everyday work.⁸ Candidates for the NPC are nominated by the CCP. Then, from this pool of candidates, about 3000 NPC deputies are elected by the people's congresses of provinces, autonomous regions and municipalities, and the People's Liberation Army. The NPC is subordinate to the Party Standing Committee and the State Council.

⁹ <http://www.cecc.gov/chinas-state-organizational-structure> (Accessed 18.36 30 January 2015)

¹⁰ China's government operates at six levels of administration. The first is made up of provincial level governments, provinces, autonomous regions municipalities, and special administrative regions. The second is 300 prefectural units. The third is the 3000 counties and county level cities, and the fourth has 40,000 townships and towns. Parallel party and government organisations and People's Congresses exist at each level. Villages are defined as 'mass organizations of self-management' and are not part of government or state administration (Lawrence and Martin, 2013, pp. 9–10). The Chinese People's Political Consultative Conference (CPPCC) - plays a minor advisory role for the state bureaucracy and legislature.

¹¹ <http://www.marxists.org/archive/lenin/works/1922/nov/13b.htm> Lenin elaborates his New Economic policy as one in which the following balance of economic forces exists. (1922)

'What is the plan or idea or essence of NEP?

(α) Retention of the land in the hands of the state;

(β) The same for all commanding heights in the sphere of means of production (transport, etc.);

(γ) Freedom of trade in the sphere of petty production;

(δ) State capitalism in the sense of attracting private capital (both concessions and mixed companies).'

¹² <http://www.marxists.org/archive/marx/works/1847/11/prin-com.htm>

¹³ http://www.stats.gov.cn/english/newsandcomingevents/t20091225_402610168.htm

¹⁴ The number of registered companies has grown rapidly ever since. In 2013 there were 12.54 million registered private companies. Their average capital was RMB 3.13 million and they employed had an average of 10 people. There were also 44.36 million individual businesses. Their average capital was RMB 54,000 and they employed an average of 2.1 people (Feng et al., 2016, p. 72).

¹⁵ http://www.china.org.cn/top10/2011-09/03/content_23345008.htm

¹⁶ <http://www.acfic.org.cn/zt/11/2011500qiang/pic/%E4%B8%AD%E5%9B%BD%E6%B0%91%E8%90%A5%E4%BC%81%E4%B8%9A500%E5%BC%BA%E5%90%8D%E5%8D%95.pdf>

¹⁷ I assume this is based on extending the concept of central state ownership to subordinate companies that are majority owned by centrally owned SOEs.

¹⁸ <https://www.ft.com/content/c67b0c05-8f3f-3ba5-8219-e957a90646d1> Accessed 27 Jan 2017

¹⁹ China's biggest state banks recruited into stock market rescue <http://www.ft.com/cms/s/0/c30b6f3a-2c3d-11e5-8613-e7aedbb7bdb7.html#axzz3gjl2F4RM> July 18, 2015 (Accessed 25 July 2015 14.15 GMT)

²⁰ For example Wangke is China's largest real estate company and it is a private company, but its largest single shareholder is a government entity (Walder, 2011a, p. 33). Huawei is a private company, but one whose ties to the military and ambiguous relationship to share issuance and recordkeeping, make its credentials as a fully private company at the very least questionable (Huang, 2008, pp. 10–12).

²¹ Data from the NBS <http://www.stats.gov.cn/tjsj/ndsj/2011/html/E0402e.htm> Accessed 20 July 2014

²² <http://www.stats.gov.cn/tjsj/ndsj/2016/html/0402EN.jpg> Accessed 20 Nov 2017

²³ The cost of listing a company is about \$3 million US a sum beyond the reach of most Chinese private SMEs. (Lin 2012:214)

²⁴ <http://www.stats.gov.cn/tjsj/ndsj/2016/html/1003EN.jpg> Accessed 1 Jan 2018

²⁵ <https://www.ft.com/content/1e798454-ce5b-11e6-864f-20dcb35cede2> Accessed 1 Jan 2017

²⁶ This was Kornai's view in 1992, before the widespread proliferation of networked computers and devices, in which intelligent feedback systems linking consumer purchases and the global production chain were developed.

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- ²⁷ From the translation of the 12th FYP by the European China Trade Project.
http://www.euctp.org/index.php?option=com_jdownloads&Itemid=19&view=viewcategory&catid=42&lang=eeu)
- ²⁸ http://online.wsj.com/public/resources/documents/NPC2017_NDRC_English.pdf Accessed 1 Sept 2017
 See http://www.chinadaily.com.cn/china/2016-03/18/content_23956775.htm for the official translation of the report.
- ²⁹ <http://www.eeo.com.cn/ens/2012/0810/231626.shtml> Accessed 12.37, 4 June 2015
- ³⁰ http://online.wsj.com/public/resources/documents/NPC2016_NDRC_English.pdf
- ³¹ PRC Constitution Article 10. Land in the cities is owned by the state. Land in the rural and suburban areas is owned by collectives except for those portions which belong to the state in accordance with the law; house sites and private plots of cropland and hilly land are also owned by collectives. The state may in the public interest take over land for its use in accordance with the law. No organization or individual may appropriate, buy, sell or lease land, or unlawfully transfer land in other ways. All organizations and individuals who use land must make rational use of the land. <http://english.peopledaily.com.cn/constitution/constitution.html>
- ³² <https://www.bloomberg.com/news/articles/2014-03-25/a-6-dot-8-trillion-price-tag-for-chinas-urbanization> Accessed 30 July 2016
- ³³ China's private coalmines <http://www.economist.com/node/14663437> (Accessed 15.25pm 20 June 2015)
- ³⁴ China Fortifies State Business to Fuel Growth
<http://www.nytimes.com/2010/08/30/world/asia/30china.html> (Accessed 15.45pm 20 June 2015)
- ³⁵ China Fortifies State Business to Fuel Growth
<http://www.nytimes.com/2010/08/30/world/asia/30china.html> (Accessed 15.45 GMT 20 June 2015)
- ³⁶ After Melamine-The Return of the State <http://www.eeo.com.cn/ens/feature/2009/11/08/155083.shtml>
 (Accessed 15.32 GMT 19 July 2015)
- ³⁷ Dr Shuanghua Bids Farewell to Rizhao <http://www.eeo.com.cn/ens/feature/2009/11/08/155083.shtml>
 (Accessed 15.38 GMT 19 July 2015)
- ³⁸ <https://www.ft.com/content/d859d86a-ae5c-11e7-aab9-abaa44b1e130> Accessed 1 Nov 2017.
- ³⁹ <https://www.reuters.com/article/us-china-corruption/chinese-watchdog-says-1-34-million-officials-punished-for-graft-since-2013-idUSKBN1CD04B> Accessed 10 Oct 2017

4. Theories of capitalist China

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4.1. Introduction

This chapter examines the literature that describes China's transformation as one from socialism to capitalism.¹ To introduce this, I select a representative sample of the dominant historical narrative in the field.²

I evaluate studies that apply "Varieties of Capitalism" (VOC) theories to China. The original VOC theory is based on a binary ideal-type model that compares and contrasts Anglo-American capitalism to Germanic capitalism. However, in this chapter the concept of capitalist varieties encompasses a broad range of theories that locate China as a type of capitalism.

I review several influential contemporary frameworks, which analyse China in an East Asian, social, cultural and historical context.

This is an approach adopted by many Sinologists and political economists. Studies of the emergence and character of the modern Japanese capitalist state generated the influential "developmental state" theory. By employing this framework, China has been compared with Japan and other East Asian capitalist states. A further conceptual outline, which defines China's system as Centrally Managed Capitalism (CMC), is also considered. This theory offers insight into the ideological predicaments confronting China's leadership, and revives questions about the basic definitions of capitalism and its dynamics. After this, I evaluate two Marxist theories of capitalist restoration in China and assess their arguments.

I question the theory that state monopoly power over the Chinese economy plays a negative role. And I consider the structure of leading multinational companies, which appear to have acquired a dominant position within the commanding heights of the world economy. Then I examine the growing influence of China's Internet giants.

Insightful as these theories are, they do not adequately identify, isolate or evaluate, the basic features of capitalism. This is crucial in deciding whether China is capitalist. Therefore, I return to Kornai's theory of capitalism and I draw on Xu Chenggang's detailed assessment of Kornai's theory of capitalism and its application to China.

4.2. China's billionaires

The scale and speed of capitalist accumulation in China is truly astounding. In February 2016 the *Financial Times* reported that China is home to 470-dollar billionaires, compared to 535 in the United States. In Greater China, including Hong Kong and Taiwan, there are 568 billionaires and their total net worth is estimated to be \$1.4tn. A grand total of 630 billionaires of Greater Chinese origin account for 29% of the world's 2188 billionaires, and these figures ignore concealed wealth.³

In China, the staggering accumulation of personal wealth by the few is a recent phenomenon. Indeed, the official ideology of the CCP remains formally committed to socialism and communism. The CCP's and China's national constitution - and all of the country's state organs - are ostensibly aligned with these objectives. The introduction of capitalist relations was supposed to be a detour undertaken to accumulate sufficient knowhow and advanced means of production, to create the material basis for socialism; which requires a well-off society based on a high per capita level of production.⁴ But China's formal, legal, and ideological structure stands in stark contrast with the reality of its super-rich elite and their intimate connections to sections of the party leadership.

The International Consortium of Investigative Journalists reports that 22,000 Chinese and Hong Kong accounts are held in tax havens. They focus on the 'Red Nobility' - relatives of politburo members - who stashed away huge sums overseas. Their business interests span every section of the Chinese economy and include state and private enterprises. The use of tax havens followed changes to laws governing the economy in the 1990s, which were designed to serve the interests of SOEs. As foreign enterprises did not trust these laws, they channelled their China related financial operations through offshore tax havens. And they also encouraged wealthy Chinese clients and partners - often engaged in illicit activities - to do the same. Thereafter, each major political and economic crisis (the Hong Kong handover in 1997, the Asian crisis in 1998 etc.) exacerbated the perceived risks to the rich, and accelerated the flow of money into tax havens.⁵

This enrichment process, and its connection to leading CCP cadres, appears to confirm the consensus in Western scholarship that China is capitalist. Indeed, so widespread is this view that the overwhelming majority of scholars of China's political economy make little attempt to define capitalism. Instead, China's transition is described by historical narratives, in which the growth of markets is equated to the rise of capitalism.

The influence and role of China's SOEs is hotly contested and the monopoly power of state-owned and state controlled enterprise groups is widely condemned inside and outside China. Critics maintain that the structure and influence of SOE monopolies is enormously costly and damaging to the overall welfare of society and to capitalism. A closely linked problem is that China seeks to nurture large state-enterprises so that they can outstrip Western multinational competitor firms.

4.3. The historical narrative of capitalist development in China

The hegemonic discourse on China's development is dominated by the school of New Institutional Economics.⁶ One of its most prominent exponents is the Nobel Prize winner Ronald H. Coase whose ideas are highly influential in debates inside China. In the book *How China became Capitalist* Coase, and his colleague Wang, (Coase and Wang, 2012), present a narrative of China's capitalist evolution that, with this or that minor shift in emphasis, can be considered as a typical overview of this process. They see capitalist ascendancy as the unintended consequence of state policy measures.

The authors employ a method of systemic categorisation, according to which: 'The most fundamental difference between capitalism and socialism is the operation of a market pricing mechanism in the former and its replacement by state planning in the latter.' (Coase and Wang, 2012, p. 168) They define China as capitalist based on the overwhelming influence of markets for goods and services (Coase and Wang, 2012, p. 197). And progress toward capitalism is defined by the degree of state withdrawal from the economy.

For Coase and Wang this process of transition in China succeeded because capitalist incentives motivated wide layers of society and these social forces overcame counter-pressures emanating from the socialist objectives and traditions of the CCP leadership. They identify four 'revolutions' that created Chinese capitalism: the spontaneous spread of

peasant incentives; the success of Township Village Enterprises (TVEs) in acting like private capitalist firms; which helped to generate a capitalist class; and finally, the creation of 'special economic zones'.

For Coase and Wang it was the emergence of a national market, spurred-on by regional competitive pressures that accelerated industrialisation. This was based on the improved dissemination of knowledge. As a consequence, all levels of government administration 'threw themselves into an open competition for investment and for good ideas for developing the local economy.'⁷ These 'good ideas' came, so these authors say, from the earnest search for mechanisms and measures that might assist modernisation. So here the driving force of capitalism is presented as competition, markets, good ideas and dreams of modernisation. However, these "good ideas" came mainly from government agents, and investments were by driven state-led visions and dreams of modernization. This contradicts the idea that profits and return on investment are the motive force of capitalism. We shall return to these themes later in this chapter when we examine the theory of Centrally Managed Capitalism.

After the death of Mao Zedong in 1976 delegations were dispatched far and wide to assimilate relevant experiences and draw lessons for China. For example, officials studied Yugoslavian and East European experiments, which permitted extensive markets to operate alongside, or within, the state economy. In 1978 a report by a top-level delegation to Japan concluded that a massive increase in commodity production was required before an egalitarian socialist system - based on needs - could be established. When Deng Xiaoping visited Japan he studied their management and technology; and in Singapore he learnt about how FDI had assisted its modernisation process. The so-called open-door policy promoted FDI, trade and exports. Coase and Wang believe that the primary benefit was the assimilation and dissemination of scientific and technical knowledge, which easily trumped the benefits of exploiting China's low-wage comparative advantage (Coase and Wang, 2012, pp. 33–36).

Coase and Wang pose the question: 'what exactly is capitalism with Chinese characteristics? In other words what kind of capitalism has China ended up with after its extraordinary transformation?' (Coase and Wang, 2012, p. 188) They reject the idea that the central defining feature of Chinese capitalism is the CCP's monopoly control of power and its aggressive economic interventionism. Rather, they focus on the lag between national productive power and endogenous innovation capacity - which they believe is reinforced by intellectual rigidity. They criticize the ideological restrictions, supported by the CCP's monopoly power, that limit the free dissemination of ideas (Coase and Wang, 2012, p. 192). In addition, China's system of compulsory Marxist education is slated for generating intellectual narrow-mindedness, which is reinforced by Chinese Marxism's claim to universal truth.

'The dearth of innovation and remaining state monopolies gravely reduces the range of investment opportunities that Chinese entrepreneurs find profitable.' (Coase and Wang, 2012, p. 193) As a consequence Chinese capitalists tend to manufacture for others rather than developing their own products. According to Coase and Wang major problems remain. Large bureaucracies depend on local knowledge, so their power to act is constrained by their lack of it. But better-informed local capitalist actors may not have the power to act.

4.4. China and "Varieties of Capitalism"

The theory of Varieties of Capitalism (VOC) originates from Hall and Soskice (Hall and Soskice, 2001). It differentiates between two basic forms of capitalism: liberal market economies (LMEs), like the USA, and co-ordinated market economies (CMEs), like Germany. The LME model is less interventionist and elevates private interests to the dominant motive of socio-economic and political organisation. The CME model operates with greater state intervention and higher social welfare provision. It focuses on long-term societal objectives within capitalism

rather than short-term profits. These pure ideal-type forms are regarded as the most efficient and effective ones.

VOC offered a means to study and influence China's institutional development as it adopted market reforms. This task was undertaken by Ahrens' and Jünemann's (2010) in their comparative survey of China's institutional dynamics, which examines China's transition from central planning to a capitalist market economy from the VOC perspective. They note that in China, incremental and pragmatic changes occurred alongside strong economic growth, and this negated the big-bang method of revolutionary destruction that was applied to much of Eastern Europe and the former Soviet Union.

By combining transition theory with a theory of how institutional forms compliment each other, Ahrens and Jünemann consider how China's comparative advantages can be enhanced. VOC theory posits universal entrepreneurial drives expressed through pressure on institutional forms and actions. However, decision-makers choose between LME or CME models but as corresponding social relations morph into comparative institutional advantages, changing VOC type becomes difficult. As China's system stems from a Maoist institutional background its transition towards either VOC type is bound to be far more complex and fraught with difficulty than changing from a US to a Germanic model. Indeed, although Ahrens and Jünemann embark on their investigation with the aim of identifying where China's institutions fit on the LME-CME spectrum they soon find that 'socialist' legacies remain ubiquitous.

When Ahrens and Jünemann compare China's financial system and its stock market to LME or CME systems, they discover that state controlled 'remnants' - state owned banks and financial institutions - dominate over non-state finance. And they blame the gradualist method of systemic transition that sustains loss-making enterprises. Nevertheless, Ahrens and Jünemann explain that less restrictive state control and greater access to inputs and markets have enabled the private sector to flourish.

But China's stock markets are hampered by price distortions, a lack of investor protection, and weak law enforcement.

An intense bargaining process between local and national bureaucracies decides which firms can be listed. Political criteria determine most bank lending decisions; information disclosure is not standardized; and accounting is opaque. High trading volumes reveal the speculative nature of China's stock market. Although shareholders can put pressure on the board of directors and influence management actions; party and state control predominates, and 'the concept of socialist "public" ownership is still prevalent in the minds of both government officials and managers' (Ahrens and Jünemann, 2010, p. 15). Party controlled state entities dominate decision-making in shareholding companies; and supervisory bodies are normally composed of 50% shareholders and 50% employee representatives. This results in a strong party presence. Supervisory boards control operations; the supervision of managers and directors, and policy changes, and they convene general meetings (Ahrens and Jünemann, 2010, pp. 16–17).

China's business relations are said to operate through mutual obligations known as *guanxi*. *Guanxi* relations are nepotistic social networks that facilitate deals between individuals, firms and government agencies, through informal ties that help to organize and structure economic relations. However, in SOEs and associated enterprises, it is the party that defines these relations (Ahrens and Jünemann, 2010, pp. 21–23). Intra-firm relations are dominated by a collectivist managerial style that Ahrens and Jünemann attribute to Confucian values of family and social order. Leaders define the general outlines of company objectives and tasks, but considerable freedom is granted to employees to bring them into being. In large SOEs, formal, hierarchical, and bureaucratic authority is the norm (Ahrens and Jünemann, 2010, pp. 25–27). So, when Ahrens and Jünemann conclude that these patterns resemble CME more than LME systems; it appears to be rather an arbitrary pigeonholing exercise, as the parallels with the socialist legacy are closer than either VOC model.

Ahrens and Jünemann accept that VOC is inadequate to capture China's economic transition. And they suggest that complementary institutions promote the transition process. For example, a combination of insecure property rights and guanxi based networks help to overcome institutional deficiencies. They say that VOC fails to account for China's political dynamics because it focuses on an actor-centred approach, in which firms are viewed as the primary creative agents, where economic policy evolves out of bargaining between individuals, firms, and their collective organisations and the government within a democratic environment. According to VOC theory institutional forms emerge out of compromises produced through this process. But the ubiquitous influence of China's Communist Party and its leaders, when elaborating and implementing various phases of transition - through the effective application of state power - contradicts this basic VOC framework (Ahrens and Jünemann, 2010, pp. 30–33).

Nevertheless, Ahrens and Jünemann believe that the VOC framework can be applied to China by making positive complementary institutional forms central to efficient markets. However, 'China challenges the conviction of the "Varieties of Capitalism" approach and economic theory in general as it shows economic behaviour is embedded in a specific social, cultural, and historical context.' (Ahrens and Jünemann, 2010, p. 33)

Whilst VOC's binary framework offers a poor match with China, the contention that there are different types of capitalism with common traits is eminently reasonable. And selecting the US and Germany as the prototype models of LME and CME systems, inevitably presents problems for comparisons with developing countries, and this problem is compounded in transition states.

4.5. Japan as a developmental model

Chalmers Johnson advanced the developmental state theory based on the Japanese experience of a highly interventionist type of capitalism. Beeson assesses its relevance to China, and McNally and Chu, and Kroeber, consider Chinese development within a wider East Asian developmental perspective.

Chalmers Johnson's developmental state theory studied Japan's state-led industrialisation and modernisation process. At its heart lies a structure of state-business relations that protects selected industrial groups. The state neither controls, nor is controlled by business interests. For Johnson it was the interdependence between state objectives and private enterprises that lay behind Japan's economic miracle - and similar patterns of industrialisation are discernable in other East Asian states like South Korea, Taiwan and Singapore (Johnson, 1999, pp. 50–59).

‘The Japanese case is actually one of an economy mobilised for war but never demobilised during peacetime.’ (Johnson, 1999, p. 41) An elite bureaucratic cadre is entrusted to select, nurture and promote, the desired industrial structure. State intervention based on market-conforming methods compliments this through investment: extensive public-private risk sharing, publicly funded research, and an administrative framework that expedites policy implementation. The key state agency is Japan's Ministry of International Trade and Industry (MITI) - a unique institution that controlled planning, energy, domestic production and international trade (Johnson, 1999, pp. 33–39). It mobilizes popular sacrifice and resources for state objectives. State authority rests on achievements that sustain the leadership's moral authority.

Japan's 'keiretsu' are privileged interlinking business groups that dominate Japanese capitalism; retired public servants take leading roles in them, which links them to state objectives. The state incentivizes

private agencies to meet state objectives, but imposes its authority over them. And social stability depends on a collectivist corporate ideology reinforced by permanent employment contracts.

4.5.1. Application of developmental state theory to China

Mark Beeson examines China from a developmental state perspective. He explains that for hundreds of years Japan and China were ruled by powerful, centralized bureaucratic states. The developmental state is created and reproduced through a historically anchored set of political relations. Beeson locates the foundation of Japan's state capacity in the promotion of capitalism after the Meiji Restoration. This completely transformed the structures of governance and institutionalized 'a powerful, centralized state at the heart of its long-run rise to prominence as an industrial and military power' (Beeson, 2009, p. 13).

US hostility to state interventionism in Japan was overcome by the Cold War it but increased after the Cold War ended. However, the self-protective responses of the Japanese bureaucracy continue to reproduce its influence, although in a less coherent and integrated form (Beeson, 2009, pp. 11–20). Beeson defines state capacity as the 'ability to design and implement policy' based on its power to penetrate and mobilize society (Beeson, 2009, p. 10). He says that China's state intervention and its emphasis on trade, emulates Japan's developmental state - as plans for socio-economic development shape resource allocation to overcome market limitations. Japan's bureaucratic agencies are intimately connected to society and to its economic actors, and this helps to prevent particularistic interests from capturing power (Beeson, 2009, pp. 9–10).

Under Mao China established a sort of 'socialist developmental state' based on centralized state planning. But by the 1980s Deng Xiaoping's reforms exposed a conflict between ideological and economic pressures. Beeson notes that the Chinese bourgeoisie today has common interests with party officials but lacks the independent identity needed to lead

society. He believes that foreign investment provided China's elite with room for economic manoeuvre, and this helped to avert the kind of political crisis that felled Communist governments in Eastern Europe and the former Soviet Union (Beeson, 2009, pp. 21–27).

China's state was disadvantaged compared to Japan, in Beeson's opinion, as its socialist heritage constrained the willingness of decision-makers to eliminate loss-making companies. Beeson identifies 'institutional inertia and the need to overcome powerful vested interests' (Beeson, 2009, p. 37) as the main problems which undermined Japan's rapid rate of progress in the 1990s and he fears that it could also do so in China today.

China's rulers lean on state enterprises and private firms to acquire resources but export based firms and foreign enterprises are less easy to control. The open markets required by the World Trade Organisation make demands on China that Japanese protectionist policies did not face. And as world production is dominated by multinationals, China is compelled to find a niche within this setting, on terms shaped by ferocious external competition that it can't control.

China's reliance on state enterprises and finance - according to Beeson - reinforces out-dated institutional relations and political forces, and acts as a hindrance to technical upgrading, industrialisation and modernisation (Beeson, 2009, p. 33). The CCP's reluctance to let companies go bust; reveals the continuing influence of vested interests - dark spectres from a bygone age - in Beeson's eyes. If they resist change, the old model will cease to be effective and the new one will not be embedded. Combining this with elements of the Western market model will inject further instability into the system (Beeson, 2009, p. 37).

4.5.2. Differences between Chinese and East Asian development

Whereas Beeson compares China to the Japanese developmental state, Mc Nally and Chu (2006) use Hong Kong, Taiwan and South Korea as

reference points to help explain China's economic development. They believe that modernisation was the initial impulse for China's economic development, but the collapse of the Soviet Union refocused political will on industrial development and economic reform. The CCP mustered its bureaucratic apparatus to mobilize resources and motivate its local cadres with market promoting incentives. And China became more open to foreign investment than Taiwan, Japan or South Korea (McNally and Chu, 2006, pp. 46–48).

It confronted developmental challenges and the transition to a market economy simultaneously. However, reform of the state apparatus 'did not establish anything resembling the Asian developmental state in terms of institutional arrangements.' (McNally and Chu, 2006, p. 49). Also McNally and Chu present the CCP's command and planning systems, and its state enterprises, as legacy hindrances to market-promoting managerial methods. Reforms to China's state bureaucracy have failed to produce institutional arrangements resembling Japan's MITI. However, they did grant local cadres a greater degree of autonomy. And this: 'generated incentives and political space for economic experimentation, which enabled China's private sector to thrive.' (McNally and Chu, 2006, p. 51).

Forms of Chinese capitalism differ by region e.g. privatized state enterprises dominate in Jiangsu province whereas Wenzhou's capitalists (in Zhejiang province) are organized on family based *guanxi* networks. They smooth relations with government cadres and help private enterprises to thrive in adversity. A large variety of state-business relations exist, but restrictions on private entrepreneurship remain commonplace; producing what McNally and Chu describe as 'the worst of feudalism, socialism and capitalism combined.' (McNally and Chu, 2006, p. 53) Despite attempts to discover common patterns between China and developmental states in East Asia. They conclude that 'the PRC has not yet developed anything akin to the developmental state institutions found in Japan, South Korea and Taiwan' (McNally and Chu, 2006, p. 54).

Like McNally and Chu, Kroeber (Kroeber in Kennedy, 2011) considers Japan, Taiwan and South Korea as appropriate comparator states for China. Kroeber examines the basis of China's economic development by considering technique, innovation, enterprise competitiveness, and political power, in a global context.

Banks in Japan, South Korea, Taiwan and China all offered credit to promote industrial policy objectives and export industries, in price-sensitive competitive markets. However, in China, planned prices remained deeply influential until the mid 1990s. And Chinese banks maintained 'uneconomic' state companies afloat, to an extent that - in Kroeber's view – would have been inconceivable in Japan or South Korea. He says China displays three major differences with East Asian developmental states: the extent of state ownership in China; the predominance of decentralized decision-making structures; and the level of positive support for foreign direct investment (Kroeber in Kennedy, 2011)

Kroeber believes that China's large private business groups are politically insignificant when compared with major Japanese corporations or the South Korea's chaebol business groups. In China state ownership dominates in large-scale industry and private ownership dominates amongst small firms. The segregation of the Chinese economy by ownership structures and sectors minimized direct conflicts between the private and state sectors. In addition, Kroeber believes the friction between state and private enterprises has been contained by offering CCP membership to entrepreneurs, and credit lines to selective private enterprises (Kroeber in Kennedy, 2011, pp. 44–47).

4.6. Centrally Managed Capitalism

Nan Lin suggests that China's system constitutes a new type of capitalism. He calls this Centrally Managed Capitalism (CMC), which is distinct from other capitalist models and may eventually be emulated elsewhere (Lin, 2011). The idea of Centrally Managed Capitalism (CMC)

was developed to explain the character of China's political economy. Lin defines capitalism as 'social institutions that sustain the production, accumulation, and reproduction of capital' in which, the institutions of capitalism are defined as 'calculating capitalists, free markets, wage labour, an expansive system, and a strong supporting state.' (Lin, 2011, p. 64)

Lin believes that two features of Chinese capitalism are unique

1. The way that the state acts as a capitalist as distinct from supporting private capitalism
2. Economic activity is nested in social relations based on guanxi based business networks

He views China as a possible trailblazer of capitalist development and suggests it may even become an alternative model for capitalism. CMC rests on party control over appointments and incentive structures; control over the reward systems in organisations and enterprises; and control of capital. Lin predicts that ideological change will eventually eliminate the influence of Marxism and replace it with Confucian ideology based on moral and ethical leadership; and stability, order, and hierarchy. And he believes this will remove the need to explain the abandonment of socialist objectives.

In pioneering countries of capitalism Lin says the role of the state was subordinate. However, the industrialisation of backward economies demanded active state intervention. Asian developmental states were autonomous and effective in defining national economic objectives, mobilising resources, and coordinating companies to attain them. Lin extends his theory to argue that a powerful state is essential in all capitalist systems. The state sets the rules governing markets and the containment of social and economic conflicts. But it must also protect capitalists to ensure their reproduction. And the state arbitrates disputes between capital and labour with a view to sustaining capitalism (Lin, 2011, pp. 64–67).

State interference in markets is commonplace, says Lin, even in the United States. It protects markets and private sector entities when they run into trouble. Regulatory frameworks are crafted to support stable social structures, laws, property rights, taxes, finance, employment relations and other key regulatory spheres. State investment in infrastructure, research, and policies that foster prioritized sectors, is also commonplace. For Lin the state is vital in all forms of capitalism so it is not a developmental phenomenon at all. Rather, he attributes unique forms of state involvement in capitalism to their historical genesis, and sees state intervention as essential during periods of economic instability or dislocation. However, as the liberal capitalist model is closely associated with the ideology of free and unregulated markets, its deregulatory tendencies tend to provoke speculative frenzies and cycles of boom and bust (Lin, 2011, pp. 67–68).

In the West, independent governance by a board of directors is the norm in major enterprises. In China the de-facto board of directors is the state. As a consequence there is greater coordination across firms in China. Personnel selection is more centralized, and the government picks and supports winners to the exclusion of competitors. The decentralized power of local governments appears to contradict Lin's CMC concept but he resolves this by reference to fuzzy relations and the need for flexibility.

The term 'state capitalism' encompasses diverse traditions and contexts. For Lin, the specific constellation of Chinese power relations and economics is unique, and it is the 'alignment and synchronization of a party-government-military-economy regime' (Lin, 2011, p. 67) that merits its own classification as CMC.

In CMC the state is an active capitalist. It creates and maintains enterprises by means of ownership and control over capital and appointments. It promotes free markets for capitalists and wage labour, and it is central to all aspects of the economy. State and private enterprises compete against one another, and the enrichment of capitalist elites is supported. However, these elites are subordinate to the

state. Workers in state enterprises, although they are not free to engage in labour unrest, are offered cosseted terms and security - similar to those of low-level state bureaucrats. National champions are selected, nurtured and supported, and the state's reward and punishment systems are applied to control the actions of leading enterprise cadres.

In its transformation away from command-based structures - China developed a new combination. This uses capitalism to generate wealth, whilst maintaining the existing CCP controlled state as the guarantor of development and stability. The party encourages experiments with markets without establishing free markets. Privatisation occurred in housing, household goods production, services and the labour market. And profit based operations, capital accumulation, and investment operates with minimal state involvement. However, the marketization process is firmly under party control (Lin, 2011, pp. 70–73).

Party interference extends into significant private sector companies e.g. the state may buy-up shares and impose its own managerial control, and family members of state officials often enter the private sector. But, the extent to which this mobility of power encompass private, public, political and economic sectors is of note (Lin, 2011, pp. 74–75).

State banks and enterprises dominate Chinese capitalism and its sovereign wealth funds are major global investors. Rapid action by state banks enforced party and state decisions in 2008-9, when China launched a massive counter-cyclical investment programme.

'More than 75% of the stimulation fund (\$586 billion) was allocated to infrastructure work, almost of all which was allocated to corporations owned, controlled, or affiliated with the state or local governments' (Lin, 2011, p. 78).

The state also receives capital from state-owned companies - not only by means of taxation. The Party's control of shareholding enterprises is ensured through appointing the managers. State enterprises are also compelled to donate money on demand. Above all the need to fulfil

planning objectives. The integrated operational capacity of the state helps its enterprises to function effectively in world markets. Chinese infrastructure and raw material deals overseas are invariably signed by state-owned companies or state-near companies. The unified nature of state actions intensified after the Great Recession (Lin, 2011, pp. 78–80).

The party controls appointments to a vast range of institutions, but permits them to operate quite independently. Local state enterprises and governments exercise considerable fiscal independence.

‘The firms, as capitalistic entities, secure and accumulate resources, organize resources in the production process, recruit cheap labour, and explore and exploit markets where they can compete advantageously.’ (Lin, 2011, p. 80)

Profit-making and market success influences decisions that guide local government-owned firms to form new enterprises and political promotion. A myriad of enterprises are created to undertake different tasks and intervene in different markets. Thus CMC reproduces itself as locally managed capitalism, which emulates the national system and operates with its own access to revenue and resources (Lin, 2011, p. 81).

4.6.1. Ideological consequences

Nan Lin's theory offered a coherent explanation of the CCP's ideological dilemmas. The party's revolutionary ideology rooted in class struggle and egalitarianism conflicts with the trajectory of development this presents major problems for ideological legitimacy. Pragmatic experimentation has defined China's path towards modernisation but economic success also caused a waning in the influence of Marxism. Two objectives were elevated to the basic props of state authority - growth and social stability. Lin examines the ideological options for the party and its dictatorship for the future and he outlines three alternatives: Western capitalist ideology; a mature form of socialism; or an authoritarian ideology rooted in Confucian traditions.

In recent years, a Confucian ideology of 'great harmony', based on good and virtuous government and prosperity, has been integrated into long-term state objectives and appears in the speeches and articles of party leaders. In such an ideology, managerial skills supplant ideological purity, as they are based on a doctrine of orderly and stable socio-economic development. However, there has been no reasoned attempt to integrate Confucian ideas with the official theory that China is at the first phase of socialism. However, Lin believes that Confucian concepts offer the party a viable alternative ideological framework with which to replace Marxism. And this is particularly relevant as the CCP has not developed conceptual perspectives about the transformation from the primary stage of socialism to mature socialism, which should correspond with advances in economic prosperity (Lin, 2011, pp. 85–88).

However, Lin notes that a veiled, and not so veiled, debate on democracy has taken place over the last decade, with senior party leaders variously defending, democracy, socialist democracy, or universal democracy, and others opposing Western multi-party systems outright. Anti-corruption campaigns play an important role in exposing the abuse of power and stemming the potential for anger to burst out into the open as generalized unrest. And nowadays there is scope for some forms of democratic expression, for example through residents associations and competitive village elections. In addition, Lin points to religious groups, which have recruited millions of people outside of state organisations. It is also noteworthy that democratic tendencies have also appeared inside the party with increasing frequency. Lin concludes that China fits a model of state capitalism - in the sense of providing its industries and enterprises with protection from world capitalist pressures. And such a form of state capitalism was applied in various developing states after World War II. China's difference lies in its genesis from state socialism and its increasingly tight control over the economy - through the party and the state. In the absence of a theory for the transition to mature socialism - and the expanded public property that this would entail - Lin believes a controlled and gradual process of enlightened

reforms will generate a more democratic form of centrally managed capitalism (Lin, 2011, pp. 89–93).

4.6.2. Capitalist China? A critique

Marshall Meyer (2011) challenges Lin's CMC theory. For Meyer, the main question is not, what type of capitalism China is creating? But 'whether China is moving towards capitalism or away from it'? (Meyer, 2011, p. 8) Meyer accepts that China's current trajectory is moving towards central management. But, having assimilated elements of capitalism, and emulated its appearance, China is pursuing a non-capitalist path.

Meyer rejects the idea that China's political economy corresponds to any comparative capitalist system. He highlights the contradiction, also flagged-up by Fligstein and Zhang (2011), that the factors which are commonly allotted a leading role in facilitating China's growth (e.g. the authoritarian state, nepotistic networks, fuzzy property rights etc.) are also held responsible for holding it back. To resolve this dilemma China's development is presented as if it were a long-distance hurdle race -where the preparation required to jump over the first hurdle, helps prepare for the next.

So Meyer says 'it is possible that China is not capitalistic, at least as capitalism is ordinarily conceived.' (Meyer, 2011, p. 7) He defines capitalism as a system where private companies govern economic activity and compete for goods, services and capital. And affirms that 'At the end of the day, a key test of a capitalistic enterprise is earnings (profits)' (Meyer, 2011, p. 8). Meyer locates profits at the very heart of capitalism. They can be reinvested, paid in dividends to shareholders and bondholders, or used as incentives for employees. Profits are what motivate private investors to invest. For Meyer, capitalism - as an ideal type abstraction- seeks to minimize the role of the state, which intervenes only as 'a last resort' e.g. to limit monopolisation (Meyer, 2011, p. 9). True, state intervention is commonplace. For example U.S. state

intervention after the Great Recession of 2008-9 was huge; and developing states often subsidize private enterprises to pursue national economic objectives.

Meyer challenges assumptions based on the unstoppable rise of private sector enterprises by differentiating between the indigenous and foreign-invested private sector. He contrasts the state sector to the homegrown private sector, and finds that the gross output by state enterprises exceeds that of the private sector, as does the amount of value added. This emulates the emphasis of Huang in his influential book *Capitalism with Chinese Characteristics* (2008). Although private firms were catching up with the state sector this process was reversed after 2008. In the colossal state stimulus package that followed the Great Recession of 2008-9, 'massive assets were infused into state owned enterprises' (Meyer, 2011, p. 10). If efficiently used, and that is a big if, Meyer believes this will enhance SOE performance and, if it is inefficiently used, it will exacerbate state sector burdens on the economy. Nevertheless, both scenarios contradict the idea that China is dominated by vibrant capitalism.

The pursuit of profit by SOEs is not primary or easily deciphered. Central government has sought higher dividends from SOEs but less than 1% of its revenue comes from this source. Managerial stock options for SOEs have been restricted, which partially decouples the pursuit of profit from managers' motivations. SOE earnings are largely impervious to scrutiny and unlisted firms rarely disclose earnings. Those listed companies that do disclose earnings are often so interwoven in complex ownership patterns (with parent, sister and child companies that are unlisted, and do not disclose their profits) that accounts can be conjured-up to reveal any desired profit rates on demand.

The central driving force of China's political economy is not profits, says Meyer, but gross domestic product (GDP) and its local counterpart gross regional product (GRP). The statistics for this are 'ubiquitous and published for four levels of the Chinese administrative system: national,

provincial, municipal or prefectural and county. GDP growth remains the most critical success measure for local officials; another critical measure is jobs.’ (Meyer, 2011, p. 11)

A major contraction of foreign trade in 2006-9 was countered by a big rise in fixed asset investment by the central and local state - mostly on infrastructure projects. State banks and state enterprises were at the centre of this process and the career incentives for officials correspond with the focus on GDP targets (Meyer, 2011, pp. 11–14). Meyer concludes that: ‘Capitalism is driven by firms, GDP growth by government. Capitalism seeks profits; institutionalized GDP growth production, employment, and ultimately, social harmony.’ (Meyer, 2011, p. 14)

From the 1980s until recent years, China's state encouraged an influx of Western foreign investment by offering cheap labour and low taxes. Now wages have risen and tax concessions are more restricted. After 2008 the Chinese state acted to ensure that the rate of GDP growth would remain at around 8%. A ‘series of interventions has brought the Chinese economy increasingly under the control of the government. China is more centrally managed today than it was 5 or 10 years ago.’ (Meyer, 2011, p. 15)

Meyer believes that centralisation in China is driven by the state's institutional drive to growth - rather than the other way around. Lin's concept of CMC is rejected for this reason, as is the general contention that China's strengths derive from its movement towards capitalism (Meyer, 2011, p. 15).

Meyer believes that the collapse of the Soviet Union portends badly for the durability of China's system and believes that a similar collapse would provoke a deep world recession. If ‘China reverts to a command economy, albeit a GDP-driven command economy rather than a Soviet-style centrally planned economy, then the possible outcomes, from the perspective of Western capitalism’...are not pleasant (Meyer, 2011, p.

16). If China continues to develop rapidly while Western capitalism stumbles 'capitalism as we know it could face a crisis of the sort anticipated by Marx and Engels' in the *Communist Manifesto* (Meyer, 2011, p. 16).. Meyer rejects speculation that Chinese state intervention is a temporary detour on the path towards capitalism, and reiterates that the central driving force remains GDP based on massive investment in fixed assets (Meyer, 2011, p. 17).

4.7. Two Marxist theories of capitalist restoration

Hart-Landsberg and Burkett (2004) and Au Loong Yu (2012) maintain that market reforms transformed China into a capitalist state. They identify the following sequential stages of capitalist restoration:

- 1) Central planning was weakened
- 2) Markets were privileged over planning
- 3) Foreign and domestic private enterprises were privileged over state enterprises (Hart-Landsberg and Burkett, 2004, p. 61).

4.7.1. Hart-Landsberg and Burkett's theory

From 1980s to the mid-1990s the decentralization of decision-making powers led state enterprises and local governments to function as profit seeking entities in markets. However, state banks engaged in excessive lending and soft-budget constraints applied. This resulted in a significant duplication of effort and overproduction, for example in the automobile industry (Hart-Landsberg and Burkett, 2004, pp. 62–65). They cite overproduction and low wages as evidence that 'China has fallen under the sway of the exploitative and anarchic dynamics of capitalist accumulation.' (Hart-Landsberg and Burkett, 2004, p. 72) However, although over-investment by state banks in state enterprises produces unsold goods, the resulting overproduction is not itself proof of the dominance of capitalism. The examples cited could instead be construed as illustrative of contradictions between local and national planning dynamics - where local interests seek to expand production without

adequately considering national productive needs, demands or efficiency.

Hart-Landsberg and Burkett define this process as market driven in the sense that enterprises faced market competition. But it is clear that state enterprises were not actually functioning as profit-making enterprises, as their operations were based on state bank loans delivered and extended on a non- or semi-commercial basis. The bad debts accumulated by many state enterprises were eliminated by the wholesale privatisation of small and medium sized state-enterprises between 1998 and 2001. This dramatically worsened the conditions for tens of millions of laid off workers. Hart-Landsberg and Burkett claim that the privatisation of these small and medium sized enterprises brought with it a dramatic fall in workers' living standards and the destruction of welfare provision for health, education and pensions. However, the real wages of urban workers employed in formal sectors have risen consistently and rapidly even during this period of mass layoffs (Ge and Yang, 2014). In addition, the recreation of new forms of welfare provision from 2003, progressive labour laws introduced in 2008, and China's social housing programme to build 36 million apartments for social housing under the present Five Year Plan, simply do not fit the trajectory that Hart-Landsberg and Burkett predicted.

China's participation in the World Trade Organisation since 2001 requires that state enterprises operate on commercial lines and without government interference. Hart-Landsberg and Burkett predicted that the eradication of the remnants of a planned economy would follow from this loss of national economic sovereignty and China would become subordinate to imperialism. Foreign and private sector investment is said to have conquered such a dominant position within the economy that: 'China's economic future now depends on the performance of privately owned enterprises' (Hart-Landsberg and Burkett, 2004, p. 58), and its growth is 'dependent on the export activities of foreign transnational corporations' (Hart-Landsberg and Burkett, 2004, p. 60). However, China is now generally regarded as an independent economic powerhouse.

Hart-Landsberg and Burkett examine the rising influence of the market and consider it to be synonymous with the dominance of capitalism: specifically foreign capitalism. The attempt to combine markets with socialism is presented as an inherently unstable state that automatically tends towards 'the full restoration of capitalism' (Hart-Landsberg and Burkett, 2004, p. 115). The main concern of Hart-Landsberg and Burkett is that any endorsement of China's development methods entails adopting criteria of success that focus on growth, and ignore the negative social impact of market relations. They believe any justification of the exploitation of China's workers undermines solidarity internationally.

The central problem with Hart-Landsberg and Burkett's approach is that it implies that Maoist autarkic economic development, between 1949 and 1979, was more successful for the mass of the people than the post Mao era from 1979 to today. This argument is based on the provision of welfare, employment and healthcare on an egalitarian basis. They also claim that economic problems evident in 1979 could and should have been resolved by greater popular participation in economic administration rather than by market mechanisms. This argument ignores overwhelming evidence of colossal improvements in life expectancy, life opportunities, and living standards for the overwhelming majority of the population since 1978. Life expectancy rose from 67.8 years in 1982 to 71.4 years in 2000 (Lu, 2012, p. 10). The withering away of the serf-like restrictions on movement that the *hukou* imposed on rural residents drastically improved the life opportunities of the peasants. The disposable income of urban residents rose from 343 yuan to 13,786 yuan and those of rural residents rose from 134 yuan to 4,140 yuan between 1978 and 2007 leading to a dramatic rise in living standards (Lu, 2012, p. 3).

Although Hart-Landsberg and Burkett assert that markets have replaced planning they present no evidence to verify their claim that planning has disappeared. Instead they simply assume that the rise of markets equals the destruction of planning.

4.7.2. Au Loong-Yu's theory

Au Loong Yu (2012) agrees with and accepts Hart-Landsberg and Burkett's basic theory of capitalist restoration. However, he acknowledges that the CCP controls political and state power based on command of state-owned enterprises (Au et al., 2012, p. 13) that 'exercise strategic control over the national economy as a whole' (Au et al., 2012, p. 21). However, they operate 'just like any other commercial company, so that today they rely more on the stock market to raise money than private capital does' (Au et al., 2012, p. 21). The dominant role of bureaucratic capital arose from privatisation and corporatisation; it controls decisions and coercive power and promotes enrichment through bribery and corruption. He says, 'the bureaucracy is the capitalist class' (Au et al., 2012, p. 14). They earn salaries and extract surplus value because the state has been privatized, and the bureaucracy owns the state (Au et al., 2012, pp. 15–19).

Au says the root of the problem lies in the fact that 'historic role of the bureaucracy acting as a substitute for a bourgeois class in modernizing the country is a contradiction in itself: it was both the result of backwardness and also its embodiment' (Au et al., 2012, p. 50). The CCP arbitrarily shaped class relations destroying landlords, creating proletarians, resurrecting the bourgeoisie, atomising the state workers, and building a new migrant working class. Only the party's exclusive rule and the objective of modernisation remained constant.

Au's says the repression of the Tiananmen protests in 1989 was a precondition for complete capitalist restoration. After this, the iron rice bowl was smashed, privatization was carried out, managerial bureaucrats plundered assets of SOEs, but the state took over the debts of these firms even as it laid-off up to 40 million workers after 1998 (Au et al., 2012, p. 25). Au says there is a 'permanent fight between bureaucratic capital and private capital over bank loans and market share.' For example, the private sector 'did not benefit from the 2008 government bailout, amounting to 4 trillion RMB' (Au et al., 2012, p. 22).

The privatisation of land generated a housing boom that the government stimulus measures after 2008 exacerbated. Accumulated debts imperil stability and consequently the national government is compelled to bail out local bureaucratic capitalism. Au believes that an economic slowdown will aggravate tensions between state capitalism and society at large, and the bureaucracy will be 'the common target of all classes' (Au et al., 2012, p. 43).

In Au's theory of bureaucratic capitalism, private and state capital is unified in the hands of CCP cadres. State property is the core of the system and it is privileged over private capital. However, Au claims that the 'planned economy has been dismantled' so it cannot be the economic regulator. However, he nevertheless accepts that the bureaucracy 'is more than capable of containing the economic cycle' (Au et al., 2012, p. 49). It invests state capital, to the exclusion of private capital, in colossal infrastructure projects, as well on subsidies to farmers; higher wages for workers; and 'massive housing projects for the poor' (Au et al., 2012, p. 41) but these are clearly not market driven imperatives. Au's method elevates bureaucratic capitalist accumulation to the dominant economic regulator. However he fails to adequately explain how or why the pressures of class conflict shape the actions of the bureaucracy.

4.8. State monopoly power

The view that China's state enterprises act as a drain on society is forcefully advocated by Sheng et al., (2015). SOEs are condemned for operating 'administrative monopolies' - defined as a business monopoly granted by government bodies. These monopolies are barriers to free entry, exit and market pricing. SOE monopolies are generally established by government entities rather than by legislation, and in real life, no power can negate decisions made in this sphere.

These state administrative monopolies evolved out of the 'planned economy era' (the Maoist period) but now the central government is dependent on the tax revenues that these state enterprises generate. Consequently, although the CCP supports the reform of SOEs it does not seek the abolition of their monopoly status. These firms retain their profits and are subject to pressure from internal interests to increase wages of workers, cadres and managers and to expand their administrative monopoly influence (Sheng et al., 2015).

Sheng et al, focus on the administrative monopoly, illegal practices, corruption, and distortions to market' prices, which distort the economy away from its market equilibrium. They claim that administrative monopolies: lower efficiency, violate social justice, and undermine the very state authority that forms them. Thus SOE monopolies at the core of the economy are seen as a threat to the rule of the CCP - not as its foundation (Sheng et al., 2015, p. xxvi).

The proposition that monopoly companies fix prices and erect unfair barriers that undermine the fluidity of market competition and efficiency, leads to the idea that the abolition of these monopolies will release wasted resources that otherwise should be used to improve the welfare of the people. Sheng and his colleagues model monopoly distortions and reveal the huge costs to each industrial sector that these distortions cause. So, for example, they say that low input prices feed into SOE monopoly profits but, if these SOEs paid normal market rates, the difference would go towards the people's welfare. As, if sales prices are set above 'natural' market rates, the savings that can be made could be spent on the people. They use this method to calculate, for example, that the telecommunications industry caused a social welfare loss of RMB 441bn between 2003-2010, and the oil industry caused a social welfare loss of RMB 1.3tn. Similarly, high-speed railway is deemed too uneconomical to justify the scale of investment it receives, because roads and slower rail connections are in need of greater investment. And they argue that state banks pocket income through exploiting deposit-lending differentials to produce excessive revenue. The cost of all this, to

the public and institutions, is estimated to be as much as US\$1.15tn in 2011 or 2.6% of GDP (Sheng et al., 2015, p. xxvii).

This extensive study attempts to calculate the scale of accumulation that can be attributed to monopolistic power derived from the administrative authority of the party-state. However, it tends to focus entirely on the negative aspects of this process. Nevertheless, the data they present can just as easily be used to provide a reference point to explain how the urbanisation and industrialisation process - driven by the state - acts to facilitate the overall economic development in Chinese society. The disadvantages of monopoly state owned industries are strongly emphasised but the benefits, in terms of the capacity to combine the resources and manpower of SOEs to meet planning objectives, are either ignored or side-lined. This is like examining someone's left hand and discussing its limited capabilities whilst ignoring the fact that the person is right handed and has two hands - which also greatly expands the potential of the left hand to engage in creative activity in combination with the right.

So perhaps the most important issue is whether the benefits of state monopoly dominance outweigh its disadvantages. And whether reforms are designed to increase benefits to society through state planning, infrastructure etc., or to serve the personal enrichment of bureaucrats or capitalists.

Global markets are already dominated by a tiny handful of private companies. So entry is not free and fair but restricted. Monopolistic enterprises can fight competitors through preferential access to credit; price wars, the manipulation of markets, political support, legal measures, and advantages in R&D etc. Cooperation between state enterprises and the party, government and state, multiplies the advantages that oligopolistic and monopolistic firms enjoy and bring to bear in order to realize state planning objectives. And it is this power and scale that permits China's SOE giants to realize colossal projects, which private companies are reluctant or unable to carry through. The unified

power of all SOEs, combined with the CCP's ubiquitous and exclusive societal organs of power and influence, can mobilize resources in ways that capitalist states are only able to emulate in wartime - when capital is controlled and subordinated to the military objectives of the nation.

4.9. Multinational monopolies and state owned national champions

Peter Nolan's (2014) analysis of the concentration of power in the hands of multinationals based in the advanced capitalist countries offers an enlightening perspective on the relative strength of China's large state and private enterprises. China sought to nurture state-owned national champions to compete with the leading multinational companies. Nolan says that these national champions operate in strategic industries, whose profile is broadly similar to the state-owned sectors established in many wealthy capitalist countries after the Second World War: banking, telecoms, oil and chemicals, aerospace, military related industries, energy supplies, metals and mining, construction. However, Nolan's passing analogy with post-1945 state intervention in Western Europe fails to take account of basic differences in the historical context. Western Europe was moving towards increasing state intervention to meet popular social objectives and to form a Keynesian type of welfare state. By contrast China's system moved from complete state dominance before 1978 to a more flexible and productive application of state economic power, which combined its universal agencies of political power. And it represents a far more ubiquitous and penetrating dominance over the economy and society than any post-war West European Social-Democratic model.

Nolan explains that China's state enterprises secure government contracts, plan for the long-term, and mutually collaborate with each other. Although multinational companies also secure access to state dominated markets, they do this through providing technology transfer. The benefits of this knowledge can be assimilated, emulated and replicated within the state sector. China's SOEs operate in designated

spheres of influence, which are protected from multinational competitors by restrictions on FDI.

The objective was to foster state giants that can surpass multinationals in important industrial sectors. In this way, China's state aerospace industry went from importing aircraft to building her own aircraft. And in the banking sector, technical and managerial systems emulated international corporate banking methods. However, many other sectors of China's economy are dominated by multinationals. Multinationals play an important role in the development of China's managerial and technical cadre - particularly those involved in the capitalist sector.

An important vanguard of China's entrepreneurial class is composed of returnees, who have studied at leading overseas universities and worked for multinational companies. Their skills, bridge enterprise cultures and enable them to apply modern international corporate practices to increase efficiency in China. The state established high-tech zones to entice talented intellectuals to return. These returnees are prominent in the corporate legal profession and facilitate the IPO process. They have assumed commanding positions within most listed companies and inside foreign multinationals investing in China. With the breakneck expansion and provision of Internet access in China many enterprises invested in related technologies, services and finance. Backed by new Venture Capital firms; several Internet entrepreneurs mirrored the meteoric rise of similar leading Internet companies internationally. The role that returnees perform fosters the adoption of global corporate governance models. Chinese returnees also occupy senior positions in several of the world's leading financial institutions (H. Wang et al., 2011).

Apple indirectly employs over 500,000 assembly workers in China and it earned \$12bn in 2011 in Greater China. Foreign enterprises dominate China's new and high-tech sectors and its industrial exports and they employ an estimated 41% of China's scientists and engineers and 37% of its high technology workforce (Steinfeld cited in Nolan, 2014, p. 752). These multinationals lie behind the modernisation of state enterprise IT

systems, and global brands dominate the production of modern consumer devices.

The widespread impression that China is a major buyer of advanced capitalist enterprises internationally is grossly exaggerated. The total stock of China's investments throughout the world stood at \$424.8bn in 2011 but Hong Kong accounted for \$261.5bn of this total. By comparison the UK's total stock of FDI in 2011 stood at \$1,700bn. Chinese FDI into wealthy countries stood at \$62bn in 2011, but total FDI into China - mainly from wealthy countries - exceeded \$712bn that year. China's investments in Singapore stood at \$10.6bn compared to \$9bn in the US, and only \$2.5bn in the UK (Nolan, 2014, p. 757). Nolan maintains that China has failed to develop state owned companies that are capable of competing with the world's leading multinational companies; and that the few firms that are globally competitive are private firms. However, more recently China has certainly increased its investments in strategically significant companies.

4.10. A new commanding heights?

Nolan believes that globalisation redefined the concept of the commanding heights of the economy through the ubiquitous spread of information and communications technology. The process of globalisation also involved privatisation, trade liberalisation, and the opening of new markets. This created leading "system integrator" firms, which Nolan says constitute the modern commanding heights or the "organising brains" of the modern capitalist corporate system.

Their operations are planned; and they exercise influence through technical, scientific, and commercial brand quality, and the huge capital at their disposal. So their economic footprint is far bigger than their nimble scale might suggest. For example, about 100 companies operating in high technology sectors account for about 60% of total global corporate R&D. Their capital and their power allows them to define the nature of technical progress and structure the character of supply

chains by pressure exerted through procurement (Nolan, 2014, pp. 750–751).

Back in 1970 the futurologist Alvin Toffler forecast that the introduction and exploitation of technology, knowledge, communications and information processing would transform society. Toffler contrasts economics based on scarcity to the inexhaustible nature of knowledge, as the use of physical objects is limited by space, whereas knowledge is intangible. Toffler explains that knowledge can be in many places at once, and it has the following characteristics: it is easily leaked; it increases with use; and small quantities can produce huge consequences. Intangible knowledge based assets are the substance of the assets of Internet giants like Google, Facebook, Baidu, etc., - enterprises, which Toffler now argues, are supplanting tangible capital. They rely on technical advances that entice consumers to become unpaid producers - like entering payment card details online, as opposed to a shop assistant taking your payment (Toffler, 2013, pp. 122–125). Toffler says that cyberspace constitutes a new continent for business, in which, Global Positioning Satellites (GPS) in outer space; streamline logistics, and increase productivity. And China's process of modernisation involves industrialisation as well as the simultaneous creation of an information society (Toffler, 2013, pp. 128–130).

4.10.1. China's Internet giants

In the last few years China's Internet giants came of age. They experienced a period of extraordinary growth in the scale of their reach and their economic influence. The first Chinese email was sent in 1987 and China's connection to the Internet took place in 1994. But by 2012, 45.8% of the population used the Internet (Yang and Mueller, 2014). China has over 688 million Internet users⁸ and is home to 4 of the top 10 Internet companies in the world. Their market valuation at the end of 2015 was: Alibaba Group (\$233bn), Tencent Holdings (\$190bn), Baidu Inc (\$72bn), and JD.com (\$48bn).⁹

Probably the most interesting is Alibaba. It operates in a way that conforms to Nolan's description of a "system integrator" company with a claim to commanding heights status. Alibaba first developed as a business-to-business portal, later it extended into consumer markets, cloud computing and finance, and it recently purchased Hong Kong's leading English language newspaper *The South China Morning Post*. Now Alibaba accounts for more than 60% of all parcels delivered in China and, through its databases, it holds a commanding lead in knowledge of Chinese consumer profiles and business patterns.¹⁰

Its foray into finance circumvents state banks, which are reluctant to lend to small and medium sized private companies. Its financial role and its mutual interconnections with the country's private enterprises allow it to champion private sector interests, and its data profiling capacity is certainly envied by the party. In 2014 it launched a programme to establish 100,000 rural service centres that allow villagers to buy and sell, and to pay for various services and utilities. In addition, it teamed up with tech-savvy migrant workers to educate and assist villagers to sell their wares etc.¹¹ Alibaba sold goods worth Rmb3tn (\$462bn) last year compared to \$341bn for the entire US ecommerce market in 2015. The stock value of China's Internet companies is amongst the highest in the world but these valuations assume that China's 668m Internet users are buying and selling on a large scale.

As most of China's Internet sales outlets do not have corresponding retail outlets, they have low operating costs and establish their online stores from scratch. This exploits the advantages of backwardness, (which Marxists call 'combined development'). This allows latecomers to adopt the latest technology without paying the cumulative costs of the historical evolution of the technology.

It remains true that some 86% of Chinese Internet users earn less than Rmb 5,000 (\$769) per month. Nevertheless sales through Alibaba's payment system - Alipay - reached Rmb12tn (\$1.9tn) in 2015. PayPal by

comparison processed a total of \$282bn in 2015. So Alipay's total accounted for over 60% of global ecommerce.¹²

In recent years China's technology, advertising and food processing industries posted rapid earnings growth, while profits at state owned industries fell by 14.5% in year to February 2016. However, profits in state controlled companies listed in Shanghai and Shenzhen fell less rapidly at 1.4%. But profits in private companies grew by 5.4%. And this growth is most evident in new economy sectors like technology, healthcare, travel and other service industries.¹³

However, China has not been an easy terrain for international Internet companies. Google pulled out of its China operations in 2010 citing security breeches and cyber attacks. In response US Secretary Hillary Clinton called for global 'Internet freedom'. What followed was unique. The government established its own search engine called Goso, which was intended to replace Google. It was later renamed Jike and merged with another state owned search engine called pangsuo (Jiang and Okamoto, 2014a). Goso was seen as a means to 'spread the Party's voice, strengthen the mainstream media's position, issue authoritative information, and showcase the Party's and country's image' (People's Daily cited in Jiang and Okamoto, 2014b, p. 92). This search engine was financed by the *People's Daily*, the official organ of the CCP. However, Jike failed to capture a dominant position in the search engine market despite state support. No other state has attempted a similarly bold move - to create a national state-funded competitor and replacement for Google. So, despite its failure, Jike represents a significant symbolic example of the ambitious measures that the Chinese state is prepared to take on the Internet, and, perhaps, in other new-economy sectors if it is deemed expedient.

Fuchs (2016) studies the rise of social media giants in China and compares them to similar US based Internet sites. He notes that Californian based companies dominate on the Internet, but 6 of the top

20 visited sites in the world are private Chinese companies listed on the US based NASDAQ market.

Baidu is like a Chinese version of Google. In 2013 it accounted for over 80% of searches in China; but Google processed 89% of all Internet searches. Over 99% of Baidu's profits come from adverts and marketing, indeed Baidu will place adverts preferentially for money. The directors of Baidu include various finance capitalists connected to other new economy enterprises like Intel, Cisco, Netflix, and GRS Ventures: these companies tend to sell services and hardware to Baidu. Like Google - whose founders own a big part of its stock- Baidu's, Robin Li, owns 31.6% of all its stock. The company pays about 15% of its profits in tax (Fuchs, 2016, pp. 21–22).

Sina Corp is also a NASDAQ listed web portal: it established Weibo in 2009, which is similar to Twitter. At the end of 2013 it had 123 million active users compared to Twitter's 240 million. Advertising and marketing made up 78.8% of Weibo's revenue. Both Weibo and Twitter experienced a period of big losses after 2008. Weibo faces stiff competition from Tencent's mobile messaging. Both Twitter and Weibo have struggled to generate sufficient revenue to justify their stock market valuation (Fuchs, 2016, pp. 24–26).

Joseph Chen founded Renren in 2005. It is similar to Facebook. In 2013 it had 206 million users, but it made a substantial loss in the face of stiff competition. It derives its revenue mainly from online games (it operates a games arm), and from advertising and marketing (through its social networking operation). The company's stock is owned by a few individuals: Chen owned 25% in 2013; and a Japanese financial company - the Softbank Corporation - owned 37.6% (Fuchs, 2016, pp. 26–29).

In Western scholarship the main narrative about China's Internet concentrates on surveillance, policing, propaganda and the enhancement of authoritarian power by the Chinese state. The coherence of this

storyline was ruptured by Edward Snowden's revelations of ubiquitous surveillance carried out by the US National Security Agency (NSA), Britain's spy agency GCHQ, as well as other intelligence agencies in Europe and elsewhere. The intimate collaboration between US Internet giants and the NSA was exposed. The post 9/11 threat of terrorism was used to justify this. Big data and personal data - all produced by users - is exploited for the profit of private companies and the security apparatus of the state. Fuchs says:

'Given these revelations, the argument that the Internet is politically free in the West and politically controlled in China has become ridiculous' (Fuchs, 2016, p. 31).

Chinese and Western social media companies commodify the personal data produced by and about consumers, and use this, to precisely target adverts for products and services. They are giant advertising companies. However, advertising spending and revenue is much lower in China than in the US.

Internet giants in China and the US are intertwined with finance capital. And even in the US return on advertising spending can be difficult to predict and can rapidly decline. All these companies are dependent on the unpaid labour that is user generated content. Some of the most prominent firms struggle to make profits and their share prices are often based on imagined possibilities, so the danger of such companies dwindling or disappearing is very real. The short history of the Internet is littered with tales of fallen giants: Netscape (search engine), Alta-Vista (search engine), Bebo (Social Network), Napster (music sharing), Myspace (social network), so there is nothing to stop some event - like a major security or privacy breach - from destroying confidence in today's Internet giants and causing a share price collapse (Fuchs, 2016, pp. 34–36).

The structure and behaviour of these private Internet advertising agencies in China and the US are very similar. This is evident in their

methods of exploitation; their financial backing; in the personal influence of company founders; and in their capitalist nature. However, collectivist influence is also evident in China's new economy and in use of social media by the working class.

Nevertheless, the CCP has total control over China's entire communications infrastructure and over the government, media, education, police, judiciary and the military. So, although Internet giants may have established mechanisms that can assume an important position within the commanding heights of the economy, they are beholden to the state tolerating their independence, which comes with strings and demands that can undermine their operations, or may force them to integrate with state-owned or controlled entities. The main objective of the government is to ensure that cyberspace and China's Internet giants cooperate to realize Party and state objectives.

President Xi Jinping made his views on the future of the Internet clear in a speech on cybersecurity and IT application on 19 April 2016.¹⁴ China's national plans for cyber development are integrated with the 13th Five Year Plan (2016-2020). Xi views information flows as a facilitator in innovation, technology, education, science, agriculture, health, governance and poverty alleviation through connecting rural areas and simplifying administration. The Party tries to ensure that expression in cyberspace does threaten stability, and yet simultaneously evolves into a means of improving administrative responsiveness to public opinion. This enables discontent to be detected early and nipped in the bud.

Government and Party officials are expected to actively participate in Internet debates and discussions to keep abreast of social moods and attitudes.

China prioritizes its cyber-independence and seeks to develop its own core Internet technologies, as otherwise, even large Internet companies can be brought crashing down. The focus on technical breakthroughs is designed to 'enhance our planning in key areas and links with a view to assuming the strategic high ground.'¹⁵

When the CCP feels threatened by the consequences of social unrest coordinated by modern communications technology, as was the case during ethnic unrest in Xinjiang Province the state has been willing to simply close down the Internet in the affected areas.

4.11. Kornai's theory of capitalism and its application to China

Kornai's book, *Dynamism, rivalry and the surplus economy* (2014) is a study of capitalism based on a comparative analysis with the socialist system. It provides a minimalist outline of the primary and essential features of capitalism, and of the consequent secondary features that this produces.

Just as Kornai examined socialism by abstracting its essential features from a study of existing socialist systems, his study of capitalism generalizes from examples of real capitalism. This distinguishes between the ideals of proponents of either system and real life systems. In this way, a non-normative scientific approach based on evidence can be employed, and theoretical abstractions can be derived from the common features of a system.

The core features of both systems are driven by 'motivations, driving forces, and behavioural regularities of the economic actors', which constitute and reproduce those "genetic programmes" that correspond to the nature of the system (Kornai, 2014, p. xii).

In the last chapter I challenged Kornai's contention that the three main characteristics of socialism no longer apply in China. However, in his recent writings on capitalism (Kornai, 2008, 2014, 2016) his emphasis shifts to focus on secondary characteristics of the system.

Recently Kornai has attempted to align his analysis of capitalism and socialism with "varieties of capitalism" theory. He categorizes his varieties according to three politico-governmental forms: democracy,

autocracy and dictatorship. However, based on historical experience, he concludes that democracy can only exist under capitalism. Socialism is restricted to dictatorial and autocratic forms because 'democratic socialism is impossible' (Kornai, 2016, p. 569).¹⁶

Chenggang Xu carried out a comprehensive review of Kornai's book *Dynamism, Rivalry, and the Surplus Economy*, which applies his theoretical analysis of capitalism to China today (Xu, 2017).

Xu explains that Kornai's systemic comparison between socialism and capitalism identifies two key distinguishing features with which to assess China's system.

1. The prevalence of a surplus economy with hard budget constraints under capitalism
2. The prevalence of a shortage economy and soft budget constraints under socialism.

Capitalism is characterized by 'excess supply, excess capacity, excess inventories and labour unemployment as long-run normalcy' (Xu, 2017, p. 2).

'In capitalism, competition creates surplus, and surplus drives firms and entrepreneurs to compete fiercely for their survival and benefits. This fundamental force drives invention, innovation, creative destruction and the evolution of capitalism.' (Xu, 2017, p. 5)

Under capitalism the competition for markets between producers and sellers generates ferocious rivalry amongst capitalists. Kornai believes this makes capitalism inherently dynamic and innovative. Innovation is allotted a key place in Kornai's systemic analysis of capitalism. The invention process under socialism is not matched by corresponding innovation, which involves 'the organization of production and the diffusion of the new product or the application of a new organizational form' (Kornai, 2014, p. 10). The main reason for the sluggish assimilation of new innovations under socialism lies, in Kornai's view, in the absence of innovative entrepreneurship.

Kornai adopts Joseph Schumpeter's (Schumpeter, 1942) view of the innovation process. According to this theory, capitalism ensures decentralized initiative, so inventors and innovators can set up a business without asking anyone for permission. Huge financial rewards flow to entrepreneurs at the cutting edge of technical progress. They are able to secure monopolistic rents even if their technical advantage is only temporary. Many entrepreneurs attempt to develop innovations; they carry out experiments, are highly motivated, and are willing to take risks. In addition, there must be sufficient flexible capital available for investment to ensure the rapid transformation of ideas into innovations and the diffusion of the products produced, including those that ultimately fail. Whilst technical progress and innovation is not always a product of the process of 'creative destruction', whereas capitalism is strongly aligned with rapid technical progress, socialism acts as a retardant to it.

To illustrate his theory, Kornai lists 111 examples of revolutionary innovations in a randomly selected, wide range of categories for products and services developed from 1920-2010. He uses this list to verify the dynamism of capitalism compared to the conservative nature of socialism. The countries producing these innovative products were USA 88, UK 7, Japan 6, Italy 2, Switzerland 1, France 1, Estonia 1, Argentina 1, Sweden 1, Denmark 1, the Netherlands 1, and the USSR 1 (Kornai, 2014, pp. 5–9). However, this list not only exposes the innovation deficit of the USSR, it also reveals the overwhelming predominance of the USA throughout the last century. Therefore, Xu qualifies Kornai's capitalist innovation model by pointing out that revolutionary new products tend to emerge only in those advanced capitalist countries where the institutional conditions that facilitate this (such as venture capitalism) are present i.e., it is not an innate condition of the capitalist system. Rather, Kornai's examples show that innovation is intimately connected to the world's dominant capitalist country.

In addition, it is certainly not always the private entrepreneur who stood at the helm of invention and innovation in the USA. Instead, huge state-led investment programmes nurtured many of the core technologies that

were the basis for the innovation edge of the USA. The reason for this is illustrated by US government support for Nanotechnology research.

'Industry generally invests only in developing cost-competitive products in the 3-5 year time frame. It is difficult for industry management to justify to their shareholders the large investments in long-term, fundamental research needed to make nanotechnology-based products possible. Furthermore, the highly interdisciplinary nature of the needed research is incompatible with many current corporate structures.'¹⁷

Nevertheless, the core argument of Kornai is that there are inherent innovation hostile tendencies within a bureaucratically planned economy. The socialist innovation processes is characterized by subservience to the central plan, and it depends on a vertical hierarchy for the approval of new initiatives. Monopolistic state owned companies do not compete for customers and the reward incentives for innovation are severely restricted. Experimental innovation is discouraged by the bureaucratic propensity to risk aversion and planned capital investment is high and consumes the available capital (Kornai, 2014, p. 21).

Xu defines China's system as 'state capitalist'. The main difference between this state capitalism and Kornai's theory of capitalism is to be found in the creative destruction process. 'Creative destruction is not only a mechanism of creating surplus; it also determines the nature of competition, the winner of the competition, eventual consequences of winning and failing, and the path of the long-term evolution of capitalism. In this mechanism, capitalism and state capitalism are drastically different. In contrast to private firms in capitalism, state firms under state capitalism continually produce and expand unwanted and obsolete products because they are protected by Soft Budget Constraint (i.e., no "destruction" policy). The monopolistic power and government protection provide SOEs with the privilege of heavily subsidized capital. They imitate other innovations at extremely low costs because of favourable technology transfer deals from advanced multinational firms that are supported by the government and the monopolized super-large scale of the market (e.g., high-speed train technology).' (Xu, 2017, p. 14)

An illustration of this process is China's steel industry, whose output exceeds that of the USA, Japan, Russia and India combined. In 2016, the government demanded a cut in steel output. This led to a rise in prices and profits. So, state owned steel makers, which dominate the industry and its suppliers, interpreted this 'price signal' as a green light to expand investment. As a consequence: 'Local officials, still hungry for growth, have dusted off their plans for big new coal mines. Officials have started to warn about a speculative bubble in the steel market. In Chinese ports stocks of iron ore, a vital ingredient in steelmaking, are near record highs.'¹⁸ The cut in production was not a horizontal response to market signals. It was a vertically imposed bureaucratic edict. In addition, cutbacks in production produced a bureaucratic solution. In state owned coal mines, rather than lay off surplus workers, or close 'uneconomic' mines; the initial response from some coal industry bosses was to reduce annual working days to 276.¹⁹

Xu attempts to resolve this problem by applying Kornai's model, which holds that four factors generate surplus under capitalism; monopolistic competition, uncertain demand, economies of scale, and the process of creative destruction (Kornai, 2014, pp. 60–67). Xu affirms that China's SOEs are oligopolies or monopolies, which compete nationally and internationally for markets. He believes that the need to compete with large private enterprises drives China's decentralized government structures to encourage their SOEs to compete on the market. This competition creates a buyers market for final goods and China's economy has a vast scale; it is the world's largest market for many products.

As distinct from market reforms in the USSR and Eastern Europe, where market forces were weak, 'the large-scale entry of non-state firms, particularly private firms, makes market competition the norm in the Chinese economy'. Therefore: 'Even SOEs, which are subject to SBC, are driven to fierce market competition and regional competition. When high-powered incentives associated with these competitions are given to

the CEOs of SOEs for market share or for profits and when SBC serves as insurance against insolvency, SOEs are induced to take bold risks in competition for market shares. This situation seems to be the force that produces extraordinary surplus' (Xu, 2017, p. 15).

However, the remuneration of SOE managers came under scrutiny in 2015 to appease discontent over high salaries in the public sector. 'Salaries for the chairmen and presidents of China's five biggest banks all dropped 50% in 2015 [...] Jiang Jianqing, chairman of Industrial and Commercial Bank of China (ICBC), the world's biggest lender by assets, made less than 550,000 yuan (\$85,000) in compensation last year. That was down 52% from 1.1 million yuan in 2014'²⁰ This salary is miniscule compared to comparable positions at international banks. In addition anti-graft measures have tightened up on many loopholes and perks. So, Xu's argument that SOE managers are motivated by high incentive-based-pay linked to the pursuit of market share and profits rests on shaky ground.

Xu shows that soft-budget constraints emerge in advanced capitalism as well as in socialism. The subprime mortgage crisis in the United States, and the associated banking crisis after 2008, is seen as a special variant of the soft-budget constraint. The subprime mortgage lenders transferred 'substantial bankruptcy risks to tens of millions of anonymous uninformed buyers globally.' (Xu, 2017, p. 15) After the global market crash, the phrase 'too big to fail' was widely employed by governments to justify immense government bailouts for major banks, which socialized their debts to save the 'system'. Xu shows that Kornai's proposition that there is an organic affinity between public ownership, SBC and a shortage economy does not apply to China, and the affinity between private ownership, HBC and a surplus economy, does not apply to the USA.

Xu's definition of China's system as one of 'state capitalism' is one in which all of the primary characteristic correspond to Kornai's definition of socialism, but whose subordinate, secondary characteristics, consist of a hybrid mixture of capitalist and socialist appearances.

Thus Xu finds that although competition exists in the market for products and services, state ownership continues to dominate the economy. And, 'in contrast to "pure" capitalism, private property rights are limited and insecure. In most important areas of the economy, the government monopolizes or controls property rights. All the land is state owned. Moreover, in the commanding heights sectors (a la Lenin's New Economic Policy), including airlines, and communication, state ownership dominates and controls the governance of state owned firms and prices.' (Xu, 2017, p. 13)

'The pre-reform socialism was a shortage economy, which is exactly consistent with Kornai's predictions. Since the reform, China transformed into a particular type of hybrid system, that is, state capitalism, similar to that in Vladimir Lenin's New Economic Policy. Indeed Chinese leader Deng Xiaoping made it clear that his reform was influenced by Lenin's New Economic Policy.' (Xu, 2017, p. 13)

4.12. Conclusion

Although the view that China is capitalist is dominant in Sinology and in the field of economics and politics, there are few studies that attempt to identify what the system of capitalism is, before they define China as capitalist. However, there are many studies that describe various elements of Chinese history, economics, social relations, politics, etc., which are, by implication, taken to be indicative of capitalistic practices. Such practices are then selected and combined to fill a basket with capitalist things from China. Although this basket of evidence may contain many elements that exist in other capitalist systems, this method elevates analogy to equivalence in its definition of capitalism.

This problem pervades the literature that I reviewed in these theories of Chinese capitalism. Coase and Wang's historical survey of Chinese reform selects markets and planning as central definitional determinants, yet Coase himself was awarded the Nobel Prize in economics for his

pioneering investigation of the firm under capitalism as a planned organization. However, it is my view that the forces identified by Coase and Wang as the motive driving forces of Chinese capitalism, such as good ideas and the desire to modernize, are not inherent to or definitions of capitalism. The resulting analysis recognizes that anti-capitalist forces continue to play a big role in the party, bureaucracy, and society. The influence of such forces is ascribed a negative role, and is attributed to 'remnants' left over from the dying system of socialism, which is assumed to have no vitality, longevity or capacity for reproduction and expansion. On the other side, the existence and widespread operation of capitalist enterprises is viewed as illustrative of vibrant and energetic new forces, whose victory is assured. I believe that such an outlook is rooted in a normative rather than a scientific basis.

'Varieties of Capitalism' theory employs Germanic and US capitalist models as prototypes and looks at institutions that differentiate these two models. These types are seen as the most successful. Attempts to compare China's system with either of these systems reveals defining distinctions that are directly connected to socialist characteristics or 'remnants' in China's system.

Those scholars, who identify China's system as a capitalist system from within an East Asian developmental state context, examine the historical development of Japanese institutional structures and those of other East Asian countries. They examine similarities and differences with China based on institutional arrangements that helped to plan their development and modernization in ways that overcame market limitations. Complexity is added to this equation by the idea that the theory of the developmental state can be applied to both socialist and capitalist states. The conclusions drawn from comparing China with other East Asian states always requires the qualification of the similarities by pointing back to the degree of China's state ownership, the SBC, and the CCP's control over society. Historical affinities; particularly linguistic, bureaucratic, and philosophical commonalities are said to be rooted in such long-term affinities.

Nan Lin's concept of Centrally Managed Capitalism is a sophisticated variant of this theoretical school. It offers explanations of state intervention designed to overcome market failures, which play a positive role in fostering economic growth, through a unique constellation of power relations.

However, differences in assessments of the inhibitory or facilitatory role of state actions reveal a widespread problem. For, if the promotion of capitalism and socialism are contradictory objectives, what are the conflicts between these systems based on? For Nan Lin this resolves itself into ideological choices between a new Confucian ideology and an as yet non-existent theory of mature socialism.

In this respect, I find Meyer's concentration on the pursuit of maximum profits for private investors as the driving force of capitalism to be a simple but valid defining and distinguishing criterion by which to assess China's system as capitalist or not. China's overwhelming focus and concentration on growth objectives is related to policies that enhance and expand the CCP and its state power. This is contradictory to capitalist profit seeking and so, when Meyer projects into China's future, a radically different non-capitalist vision emerges.

Au and Hardt-Landsberg's historical presentation of China's abandonment of socialism both derive from Marxist traditions, which should permit of clear systemic definitions. Instead, I find they produce rather formulaic concepts, which are imposed on China's reality. The resultant conclusions and projections produce inconsistent and verifiably incorrect assessments of China's recent past, despite their understandable moral outrage at the lot of the poor and the proletariat. However, as their conclusions are underpinned by rose tinted impressions of a lost egalitarian world under Mao Zedong, their arguments also lack potency.

Nolan's focus on the global dynamics of investment by multinational companies, and the technical, organizational and scientific dominance of modern 'system integrator' companies offers a valuable counterbalance to much of the hyperbole about China's rise and its supposed impending dominance of the world economy. His analysis also indicates the centrality of such firms in shaping the global economic trajectory, and argues that China lags significantly behind in these spheres. The emergence of similar firms in China in the recent past, begs the question, what is their potential to act as the pioneering champions of a modern and innovative capitalist class in China? Is this a class that will be able to gain dominance over the economy, influence opinion, change politics, and remould the state in its interests?

I point to the cyber-policies of the Party and state to show that the CCP is cognisant of the threat posed by these entities and by the Internet, to its power and prestige. Indeed, it takes active measures in these spheres, whose scope and ambition is both bold and all encompassing.

Having considered this sample of theories of Chinese capitalism, I return to the ideas of the main protagonist of this thesis, János Kornai. His own interpretation of Chinese capitalism is assessed, as is Xu Chenggang's review of Kornai's theory, which provides a penetrating insight into the advantages and problems that emerge when applying Kornai's theory to contemporary China. This returns us to the political economy of a society in which the commanding heights of the economy are in state ownership but where subordinate private activity and markets are permitted and yet are simultaneously contained by the 'Leninist' party and state, as during the Soviet New Economic Policy. This framework is investigated in depth in the next chapter.

¹ It is also important to note that nearly all scholars who identify China as capitalist today identify China as socialist pre-1976. I dispute both definitions. Indeed, the CCP says that China is currently at the 'primary stage of socialism' and, therefore, earlier definitions of China as socialist were inaccurate as they ignored the country's material backwardness. General Secretary Zhao Ziyang promoted the theory of the primary stage of socialism in 1987 at the 13th Party Congress, but Mao had earlier proposed a similar theory in 1958.

² This relies on the work of Roland Coase (1910-2013) and his Chinese colleague Ning Wang 'How China became capitalist' (Coase and Wang, 2012). Coase was awarded the Nobel Prize for economics in 1991.

³ Beijing eclipses New York as billionaire capital Financial Times <http://www.ft.com/cms/s/0/76e8a3f8-db8c-11e5-98fd-06d75973fe09.html> Accessed 11:05 26 Feb 2016

⁴ In 1984 Deng Xiaoping the initiator of China's reforms said: 'What is socialism and what is Marxism? We were not quite clear about this in the past. Marxism attaches utmost importance to developing the productive forces. We have said that socialism is the primary stage of communism and that at the advanced stage the principle of from each according to his ability and to each according to his needs will be applied. This calls for highly developed productive forces and an overwhelming abundance of material wealth. Therefore, the fundamental task for the socialist stage is to develop the productive forces. The superiority of the socialist system is demonstrated, in the final analysis, by faster and greater development of those forces than under the capitalist system. As they develop, the people's material and cultural life will constantly improve. One of our shortcomings after the founding of the People's Republic was that we didn't pay enough attention to developing the productive forces. Socialism means eliminating poverty. Pauperism is not socialism, still less communism.'

'Given that China is still backward, what road can we take to develop the productive forces and raise the people's standard of living? This brings us back to the question of whether to continue on the socialist road or to stop and turn onto the capitalist road. Capitalism can only enrich less than 10% of the Chinese population; it can never enrich the remaining more than 90%. But if we adhere to socialism and apply the principle of distribution to each according to his work, there will not be excessive disparities in wealth. Consequently, no polarization will occur as our productive forces become developed over the next 20 to 30 years.'

<http://www.china.org.cn/english/features/dengxiaoping/103371.htm>

⁵ See: <http://www.icij.org/offshore/leaked-records-reveal-offshore-holdings-chinas-elite> Accessed 12.31 GMT 7 Mar 2016

⁶ New Institutional Economics studies the way that institutions - laws, rules, customs, and norms - facilitate or hinder growth.

⁷ See <http://www.cato.org/policy-report/januaryfebruary-2013/how-china-became-capitalist> Accessed 7 March 2016 13:00 GMT

⁸ <http://www.forbes.com/sites/melanieleest/2016/01/25/chinas-nearly-700-million-internet-users-are-hot-for-online-finance> Accessed 14:12 GMT 1 April 2016

⁹ http://www.chinadaily.com.cn/business/2015-12/11/content_22686526.htm Accessed 14:27 1 April 2016

¹⁰ <http://www.economist.com/news/leaders/21573981-chinas-e-commerce-giant-could-generate-enormous-wealthprovided-countrys-rulers-leave-it> Accessed 14:42 1 April 2016

¹¹ <http://www.wired.com/2016/02/alibaba-is-training-people-in-rural-china-to-shop-online/> Accessed 15:11 1 April 2016

¹² <http://www.ft.com/cms/s/0/66ae03d0-f175-11e5-9f20-c3a047354386.html> Accessed 16:17 12 April 2016

¹³ <http://www.ft.com/cms/s/0/81da2f02-f62b-11e5-9afe-dd2472ea263d.html> Accessed 16:42 12 April 2016

¹⁴ <https://chinacopyrightandmedia.wordpress.com/2016/04/19/speech-at-the-work-conference-for-cybersecurity-and-informatization/> Speech by Xi Jinping 19 April 2016 Accessed 10 Dec 2017

¹⁵ *ibid*

¹⁶ It is unclear why Kornai is unwilling to countenance the idea of 'varieties of socialism', that might transcend one party bureaucratic rule. Indeed, perhaps the self-management tendency (2007, pp. 461–473) and the revolutionary transitional era (2007, pp. 26–30) studied by Kornai should both merit designation as 'varieties of socialism' that fit within his systems paradigm? After all both forms have existed as real systems at one time or another.

¹⁷ President's Committee of Advisors on Science and Technology, PCAST, November 1999, cited in Motoyama, Appelbaum and Parker, 'The National Nanotechnology Initiative'. Cited in (Mazzucato and Demos (Organization : London, 2011, p. 86)

¹⁸ <https://www.economist.com/news/leaders/21728640-investors-have-been-cheered-sweeping-cutbacks-they-should-look-more-closely-making-sense>

¹⁹ *ibid*.

²⁰ <https://www.reuters.com/article/china-banks-pay/update-2-china-bank-chiefs-already-low-pay-cut-in-half-even-as-problems-mount-idUSL3N1781X0>

5. Preobrazhensky's theory of socialist development

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5.1. Introduction

Evgeny Preobrazhensky (1886–1937) was a prominent Soviet economist in the 1920s. He sided with Trotsky and the Left Opposition within the Communist Party, and developed a method to investigate the contradictions that shape socialist economic policy in a backward country.

János Kornai recognizes that when a sharp debate on the character of growth in the Soviet Union took place in the 1920s: 'one of the foremost economists on the "left-wing," Preobrazhensky, put forward the notable theory of primitive socialist accumulation.' However: 'By a tragic irony of history, Preobrazhensky and many exponents of his ideas fell victim to the terror of Stalin, who then went on to implement some components of his recommendations in a way even Preobrazhensky probably did not envisage.' (Kornai, 2007, p. 198 [1992]) This chapter is dedicated to

explaining what Preobrazhensky actually *did envisage*.¹ It examines the historical circumstances in which his ideas were debated and the way that *some components of his recommendations were implemented*.

I will argue that Preobrazhensky's theory is particularly relevant for understanding the macro-level dynamics of China's political economy during the reform era. Preobrazhensky's theory offers an alternative and supplementary explanation for the growth dynamics of socialist systems to that worked out by Kornai. Where Kornai regards reform socialism as an incoherent and contradictory system that tends automatically towards disintegration, using Preobrazhensky lens, it can be understood as part of the necessary and unavoidable dialectic of socialist development in a backward economy, which involves the articulation of two systems under the dominance of public ownership and planning.

Preobrazhensky's book *The New Economics* (Preobrazhensky, 1965), first published in 1926, develops a Marxist theory of the economic law governing the transition from capitalism to socialism. Preobrazhensky calls this *primitive socialist accumulation (PSA)*.² This proposes that socialist economic policy must consciously organize the accumulation of state capital from pre-socialist sectors of the economy. This extraction of a surplus from the pre-socialist economy means exploiting the capitalist sector and the so-called "individual economy" of peasant production, until, through investing the surplus extracted in this way, the economy comes to outstrip world capitalism.

The chapter begins with a historical section, which examines the rise and fall of the New Economic Policy in the Soviet Union. This contextualizes the ideas that were debated and discussed, and reveals the nature of pressures from emergent bureaucratic forces that assumed a leading role in society. This led to the abandonment of the NEP and its replacement by tighter state control, widespread nationalization, and bureaucratic state planning and, in turn, established the system that Kornai defines as classical socialism, and others, like Trotsky, referred to as Stalinism.

Karl Marx's theory of socialism presupposes a society based on advanced technique, high productivity of labour, and an abundance of wealth. In order to identify the consequences that follow from the material backwardness of the Soviet economy, Preobrazhensky adjusted Marx's concept of capitalist and socialist transition to account for the transformation from backward capitalism to socialism. I dedicate considerable space to an exposition of this framework and method, because it examines an economy based on a combination of capitalist and socialist economic forces, in which the dominant levers of state and economic power are governed by planning. However, in these circumstances, the character of planning is also shaped and amended by the influence of the weak economic base vis-a-vis world capitalism. Preobrazhensky's theory of Primitive Socialist Accumulation is based on this set of circumstances and the complexities that flow from this. His analysis was not simply an assessment of what was, but of what policies should be consciously pursued.

5.2. The Soviet context in the 1920s

The theory of Primitive Socialist Accumulation (PSA) took centre stage during the "Soviet industrialization debate". It proposed that the socialist sector of the economy exploit the private economy to catch-up with advanced capitalism. The theory was subject to ferocious criticism, distortion and misrepresentation, and the debate was eventually resolved by violent means: through the repression of inner-party opposition in 1927, and the forced collectivization of the peasantry after 1929.³ These measures, along with universal nationalization, and the introduction of the Five Year Plan in 1928, established the 'classical socialist system' that Kornai comprehensively describes.

Karl Marx believed that early capitalist accumulation was accelerated by means of forced and unequal exchange with pre-capitalist economic formations, a process that Marx called "primitive accumulation". Preobrazhensky's theory of PSA was a modification of Marx's analysis of the genesis of capitalism.

Preobrazhensky drew an analogy in which the accumulation funds for socialism would come from unequal exchange with pre-socialist economic formations. Economic backwardness defined Soviet developmental dynamics and produced the contradictory co-existence of capitalist and socialist laws of motion, which were the object of theoretical analysis and the subject of conflicts over practical policy. Contradictions between these economic laws appeared as conflicts between industry and agriculture, and the proletariat and peasantry.⁴ These dynamics were manifest through dislocations in economic development and clashes between the interests of social classes. Preobrazhensky supported rapid capital accumulation by state-owned⁵ heavy industry, which would come mainly at the expense of the peasantry.⁶ He hoped that rising peasant incomes, rural investment, and material support from successful international revolutions would ameliorate this exploitation (Filtzer, 1979).

In the mid-1920s, as the Soviet economy approached its pre-revolutionary capacity; Preobrazhensky emphasized the need for large-scale capital investment, which would entail sacrificing present day consumption for future benefits (Erich, 1950, pp. 66–68). He thought that the gap between world market prices and those of indigenous state industrial price policy should gradually improve the industrial purchasing power of the peasantry and simultaneously maximize the flow of resources towards investment. Once such capital-intensive investment bore fruit it was hoped that the living standards of peasants and workers would consistently improve (Erich, 1950, p. 74).

For Preobrazhensky a socialist planned economy must limit and control the influence of the law of value. However, he understood that forecasting in a centralized economy created scope for grave errors to radically impact the economy - as compared to capitalism - where private interests adjust markets and counter-balance planning.⁷ Therefore economic guidance and forecasting would require a scientific theoretical method to help predict the consequences of planning in advance (Preobrazhensky, 1965, p. 6).

Before 1917 the majority of Russian Marxists held the view that a bourgeois-democratic revolution would precede a socialist revolution.⁸ One exception was Leon Trotsky whose theory of 'permanent revolution' posited that the bourgeois revolution would pass uninterrupted into a socialist revolution. In his view, the development of the productive forces produced a contradictory correlation of class forces, where a powerful and militant working class faced a weak indigenous bourgeoisie tied to the Tsarist state and foreign capital. He thought the working class would overthrow the Tsarist state, and the bourgeois and socialist tasks of the revolution would be combined and become part of an international socialist revolution (Trotsky, 2007, p. 33 [1931]).

The Revolutionary Foundation 1917-18

In the first months after the revolution, radical changes were decreed e.g. peasant land seizure, workers' control of industry, nationalization of essential enterprises, and the promotion of international revolution. This combination of revolutionary democracy and internationalism sought to strengthen internal cohesion and weaken external threats. But soon problems caused by economic dislocation were used to justify replacing autonomous workers' organizations with hierarchical authority structures. Lenin's hope for pressured collaboration with private capital was undermined by the ferocity of class conflict - as capitalists and old bureaucratic forces aligned themselves with the counter-revolution and were expropriated (Howard and King, 1989, pp. 290–292).

War Communism 1918-21

War Communism led to general nationalization, forced requisitioning and rationed resource allocation, the suppression of markets and trade, and the repression of democracy and political opposition. Bukharin theorized this practice – concluding that strict self-discipline and centralization is essential to military victory and proletarian rule. In his view, global economic decline would be followed by revolution, but this would be accompanied by further economic regression and civil war. The

overthrow of capitalism would replace economics with the conscious pursuit of proletarian interests - administrative controls would replace wartime confiscation, and regulate the relations between town and country. However, sharp class conflicts alienated the peasantry and weakened state and party power. Nevertheless, Bukharin's theory remained influential within the party and leadership even after military victory (Howard and King, 1989, pp. 292–294).

5.3. Rise and fall of the New Economic Policy 1921-29

In 1918 Lenin used the term 'state capitalism' to characterize an economic system in which capitalist enterprises of various types worked under the control of the proletarian state. The core 'commanding heights of the economy' were composed of state enterprises and trusts, which he described as being 'of the consistently socialist type'. After 1921, small enterprises were privatized, foreign investment was encouraged, and diplomatic relations were improved. Lenin exhorted communists to learn to trade, and supported emulation of capitalist methods by state enterprises to improve productivity. This included one-man management, profit calculation, and large wage differentials. He also warned that bureaucratic forces were steering the state, but hoped that party purity would be able to sustain the revolution and, if industry developed alongside peasant cooperation, the NEP could herald economic progress.

Bukharin advocated industrial advance at a 'snail's pace' based on encouraging peasant demand for consumer goods produced by state industry. He believed that an enduring worker-peasant alliance should avoid excessive demands being placed on agriculture. For Bukharin, the leading role of the workers meant class relations were based on a harmonious unity, and socialism could be realized within national boundaries. Agricultural growth would increase peasant consumption, stimulate light industry, and increase demand for heavy industry.

Leon Trotsky's view was that socialism in one country was a reactionary doctrine. International capitalism was not stable, and revolutions were likely in the near future both in Western Europe and in certain less developed countries. He believed that if his theory of 'permanent revolution' were correctly followed, the opportunities that would arise could lead to revolutionary victories internationally. Also, the economic interests of European powers would foster trade relations with the USSR, and this could be used to integrate with the world market, import goods in short supply, and utilize national comparative advantages to acquire resources for state industry. To overcome the impact of the world law of value, the efficiency of Soviet industry would have to reach that of world capitalism. Trotsky saw political reform as the primary means of changing policy e.g., to permit criticism and rank and file control over the party and the bureaucracy.

Stalin argued that splits between imperialist powers would prevent successful military intervention to overthrow the revolution and Soviet diplomacy and the Comintern could be used to neuter future threats. In the mean time, socialism could be built in the Soviet Union without the need for revolutions in other countries. For Stalin, the internal balance of forces would not lead to a life or death crisis, and thus Trotsky had 'underestimated' the peasant.

Preobrazhensky considered the rate of growth of the state vis-à-vis the non-state sector to be decisive. Rapid industrial growth could increase the consumption of peasants and workers; and increasing the strength of the proletariat, while weakening the wealthy peasants and traders, could help to maintain the alliance between the workers and the mass of peasants. However, large fixed investment was needed to outstrip pre-revolutionary production and to secure growth into the future. So, Preobrazhensky's sequencing projections were based on extending capacity to facilitate the manufacture of industrial consumer goods and alleviate the goods famine. His proposals were based on technical grounds rather than a fetish for heavy industry. Whereas Preobrazhensky advocated systematic planning to forecast and anticipate disproportions

and crises, Bukharin emphasized market autonomy (Howard and King, 1989, pp. 294–309).

5.3.1. The Left Opposition

Trotsky formed the Left Opposition in 1923, to oppose bureaucratization of the party, encourage democratic rejuvenation through workers' democracy, and promote economic planning. Preobrazhensky campaigned for the adoption of planning in the state sector of the economy. He argued that outbreaks of workers' unrest in urban areas revealed the need for the party to restrict the growth of capitalist tendencies generated by the NEP in order to meet workers' needs.⁹ The Left Opposition feared that concessions to petty bourgeois moods could act as a springboard for a reactionary authoritarian movement - drawing parallels with the period in the French revolution known as Thermidor. However, the expulsion of Leon Trotsky and the United Opposition¹⁰ in 1927, was followed by an increasingly ferocious campaign against rich peasants. In 1929, an accelerated industrialization drive by the party and state, effectively identified the entire peasantry as a hostile bourgeois class - as the hoped for wedge between the poor, middle and rich peasants failed to materialize (Carr, 1971, pp. 419–429).

The construction of the new state and society changed the functional role of the revolutionary party. Its proletarian credentials diminished as it assumed governing roles, with associated material privileges. Only a minority of party members had experienced pre-revolutionary struggle. Migration and urbanization changed the composition of the proletariat, and disappointment with the results of the revolution in everyday life, generated passivity. A small minority of enthusiastic proletarians threw themselves behind the constructive work of industrialization, but few workers responded to appeals by the Left Opposition to engage in a new struggle for revolutionary ideals, or to stand up for the opposition when they faced expulsion and exile (Carr, 1971, pp. 430–434).

5.3.2. The rise of the bureaucracy and the plan-market conflict

In the mid-1920s the debate about the rate of growth and proportionality between sectors was initially one in which the Left Opposition advocated increased industrialization broadly along the lines of Preobrazhensky's New Economics, and the party majority remained tied to the idea of gradual industrialization based on market laws, which was justified on the basis of the sanctity of the worker-peasant alliance. The arguments of the party majority shifted following the expulsion of Trotsky and his allies in 1927. This had two main impulses. The first was the perceived defence needs of the state, and the second, the dynamic of pressure stemming from the expansion needs of heavy industry.

Talk of forced industrialization and of finding the shortest path, to catch up with and overtake the advanced capitalist countries, became commonplace in the press, publications and at meetings etc. The political defeat of the Left Opposition in 1927 facilitated this, as the administrative and bureaucratic strata of the heavy industrial lobby won more influence, authority and power.

Concerns about the impact on the peasant-worker alliance of the lag in consumer production found some echo, in particular with Bukharin. Although market equilibrium theories were widely accepted within the party in 1927, strains between planning and market concepts of development were tested to the maximum. On the one side, pressures were brought to bear on the recalcitrant peasants, and on the other, great efforts were applied to ensure that consumer goods production rose, to limit the impact of this. In January 1928 consumer goods production was 26% above that of a year earlier.¹¹

Bukharin presented the conflict with planning as one of imaginary visions and plans - which he called 'bricks of the future' - against market realities and their expedient needs. Debate on the tempo of development dominated party discussions in 1928. The momentum developed by increased investment in heavy industry, heightened the confidence and

authority of its apparatus and associated officialdom. A bridge between these arguments was temporarily found in common hopes for productivity and efficiency gains. However, by the end of 1929 Bukharin's arguments were labelled by Stalin as representing the kulak and the petty bourgeoisie. The concept of planned management, along with the ideal of rapidly catching up with, and overtaking advanced capitalism, became official policy (Carr and Davies, 1969, pp. 271–332).

5.3.3. Tensions over agriculture

From 1925-1927 party and state policy had reluctantly favoured individual 'capitalist' peasant forms of agriculture. The United Opposition advocated policies supportive of voluntary cooperation, intended to unify the interests of poor and middle-income peasants with state industry. Pressure to concentrate resources on heavy industry intensified, requiring long-term investment. This meant that consumer goods production, which otherwise might have enticed the wealthier peasants to sell their grain, was deprioritized exacerbating a goods famine. The mechanization and technical advances in agricultural production improved output regardless of ownership form, and this appeared to offer an alternative to political conflicts over class interests within the peasantry. However, the larger the farms, the greater the benefits, therefore control over large farms was fundamental. The peasant response to the consumer goods famine was to hoard grain as their store of wealth, and so the wealthier farms had greater power of resistance. The state could only rely on state farms to provide and sell grain on official terms. Thus the conflict with rich peasants was revived. However, the state appeared as an alien force seeking to wrest control from the villages, where its anti-kulak policies were generally regarded as anti-peasant.

In early 1929, Stalin concluded that urban grain requirements could only be secured by forceful measures against wealthier peasants, a widely held view within the party. Fear that the kulaks would reorganize the economy towards capitalism gained adherents. It was hoped that class

struggle in the countryside would unify the middle and poor peasants against the kulak, but party organization in rural areas was weak, and kulak agitation against outside interference tended to unify the peasantry against the party. Workers' brigades were dispatched to support and encourage collectivism in the countryside as Stalin's new policy to liquidate the 'kulaks as a class' was adopted in the summer of 1929. A drastic and radical shift to rapid and forced collectivization became policy at the end of 1929. This was the result of persistent grain collection crises, the exhaustion of measures against the kulaks, and a drastic rise in black market food prices, which threatened urban food supplies and jeopardized industrial expansion plans. A flickering faith in the potential to combine collectivization with mechanization, helped to summon up hope out of desperate circumstances for the final catastrophic dénouement (Carr and Davies, 1969, pp. 237–270).

5.3.4 Preobrazhensky's capitulation

After Stalin imposed forced collectivization on Soviet agriculture many of the Trotskyist critics of Stalin capitulated to his rule. Some saw Stalin's policies as the implementation of the policies that they had advocated. Preobrazhensky was expelled from the Communist Party in 1927. He capitulated to Stalin and was readmitted in 1929, then was re-expelled in 1931, and again readmitted. Finally, he was executed in secret in 1937. His last major appearance was at the Seventeenth Party Congress in 1934. As Alec Nove shows, Preobrazhensky used the opportunity to make what was almost certainly a veiled attack on Stalin's policies. He condemned his own previous proposals saying: 'I thought that by exploiting the peasants, by concentrating the resources of the peasant economy in the hands of the state, it would be possible to build industry and develop industrialization.' (Cited by Alec Nove in Preobrazhensky, 1965, pp. xiv–xv)

Preobrazhensky explained that Marx and Engels had not solved the question of the village economy under socialism, and Engels maintained that collectivist agriculture would emerge only gradually. However, thanks

to Stalin's "remarkable far-sightedness," the problem was finally resolved - by force! However, Preobrazhensky's speech was crafted in such sycophantic language that it disarmed Stalin's supporters, but the underlying message was clear. Stalin's collectivization had carried through a form of primitive socialist accumulation in a single blow, to force industrialization. Stalin's unique "contribution" was the violent way it was carried out (Alec Nove in Preobrazhensky, 1965, p. xv).

5.3.5. The victory of planning

The eventual ascendance of planning was not simply the result of an ideological clash or a battle between social classes. Planning emerged from within the commanding centres of administrative power. Initially, forces in favour of planning were segregated, spontaneously emerging from below. By the mid 1920s diverse agencies expanded the nature and depth of their activities. Planning impulses arose from within institutions governing finance, industry and government at various levels of hierarchal and geographical authority. They automatically groped towards planning, and their decision-making powers expanded, as infrastructure, enterprises and institutions at the centres of power grew in scope and influence (Carr, 1958, pp. 490–518)(Carr and Davies, 1969, pp. 787–897). For example the expansion plans of the vehicle industry, particularly tractor production, escalated in scale and significance in the late 1920s. Eventually, the centrality of these sectors to state objectives resulted in discussions and decisions about daily operational and organizational details of factory and industrial policy being taken in meetings of the leading bodies of the party and state.

The victory of planning over markets was, in one sense, a vindication of Preobrazhensky's theoretical contention that a clash of fundamentally counterposed forces characterized the NEP. However, the use of extreme violence and the rapidity of execution was a clear and unequivocal deviation from his approach. This produced the expropriation of the means of production of practically all non-state economic entities in a single blow, which meant that the exploitation of

the private economy was closed off prematurely, before its potential was exhausted, and before collective forms were able to outstrip them in productivity.

5.4. Preobrazhensky's definitions of political economy

I now turn to the task of describing Preobrazhensky theoretical approach in depth. In this section I present his definitions and categories.

Political economy is the science of the laws of development, equilibrium and decay of the commodity, and commodity-capitalist mode of production. Its fundamental categories are commodities, the law of value, wages, surplus value, profit, price and rent.

The **commodity** expresses the type of general production relations where markets bind together independent commodity producers.

Economic laws produce 'a constancy of results following from the reproduction of a certain type of production relations.' (Preobrazhensky, 1965, p. 57) **Political economy** studies these relations between people in the process of capitalist production and 'the types of regularity inherent *only in this form*, the types which reveal themselves on the basis of the operation of the law of value.' (Preobrazhensky, 1965, pp. 48–49)

The **law of value** is the 'law of spontaneous equilibrium of commodity capitalist society. In a society without commanding centres of planned regulation, thanks to the operation of this law, directly or indirectly, everything is achieved which is needed for the comparatively normal functioning of a whole productive system of the commodity-capitalist type: the distribution of productive forces - that is, people and means of production – among the different branches of the economy; the distribution of the product of society's annual production between workers and capitalists; the distribution of surplus value for expanded reproduction between different branches or countries, and its distribution among other exploiting classes; technical progress; the victory of

advanced forms over backward ones and the subordination of the latter to the former' (Preobrazhensky, 1965, pp. 147–148).

The operation of the law of value means that 'aims, plans, aspirations, and expectations of the agents of production' (Preobrazhensky, 1965, p. 49) cannot foretell the actual results. The absence of a planned distribution of the productive forces means that the law of value manifests itself blindly as if it were a law of nature.

'**Wages** and **surplus value** are the essence of the relations of production and distribution between workers and capitalists. The category of **profit**, as another form of surplus value, is a relation of distribution between capitalists, which passes thanks to the mechanism of the equalization of the rate of profit and the entire mechanisms of capitalist society into a relation of distribution of labour and means of production.'

(Preobrazhensky, 1965, pp. 148–149)

Prices express labour productivity and distribution and act to redistribute productive resources between economic branches, shaping the flow of values within society. Rent is a redistributive relation between tenants and owners that transfers part of the surplus value to the latter.

Capitalism is an unorganized spontaneously equilibrating system in which human relations are materialized. Its laws appear as accidental events and can only be grasped by critical and abstract analysis of fundamental and pure systemic features, which reveal its specific regularities. Marx developed his theory of abstract capitalism, within which real capitalism 'lives and moves' to provide the means to understand its laws of motion (Preobrazhensky, 1965, pp. 43–48).

Preobrazhensky describes Marx's model of capitalism as "theoretically photographed" in 'pure form in its native spontaneity' (Preobrazhensky, 1965, p. 150). But this pure form never existed in reality; the influence of large enterprises and banks and the rise of **monopoly capitalism** amended the law of value by restricting spontaneous competition.

Monopolies could push prices above their value or drive out competition by dumping. Their collective power altered economic dynamics and the laws of political economy. A number of capitalist countries introduced state planning, including price controls, the regulation of surplus value, and the redistribution of productive resources.

Preobrazhensky believed that this indicated an objective tendency for socialized production to replace capitalism, and laid the basis for socialist production provided the working class came to power. He cited German “state capitalism” in the First World War as an example where commodity production was planned in key sectors, free competition was curtailed, ‘and the working of the law of value in many respects was almost completely replaced by the planning principle of state capitalism.’ (Preobrazhensky, 1965, p. 153)

5.5. Capitalism, socialism and accumulation

Preobrazhensky distinguished between methods by which capitalism surpassed feudalism and those a socialist economy could use to develop socialist capital. Capitalism accumulated and established a commodity economy within feudalism before bourgeois revolutions took place. Capitalist manufacture displayed superiority over craft production based on a few advanced enterprises. Its economic conquest occurred spontaneously and the export of capital stimulated capitalist economic development in petty-bourgeois economies. Capitalism also accumulated by means of primitive accumulation, the unequal exchange of goods, and the seizure of resources from pre-capitalist economic formations and nations, e.g., through the slave trade, exchanging cheap manufactured goods for gold, seizing common lands, etc. In contrast, socialist production can only begin after the seizure of power, and it can only conquer other countries by means of revolution (Preobrazhensky, 1965, pp. 79–80).

‘The nationalization of large-scale industry is also the first act of socialist accumulation, that is, the act which concentrates in the hands of the state

the minimum resources needed for the organization of socialist leadership of industry.’ (Preobrazhensky, 1965, pp. 80–81)

For Preobrazhensky **socialist accumulation** refers to surplus product produced for the self-expansion of the means of production of the socialist economy. This requires highly developed technique, organization and productivity of labour, corresponding with high capital intensity. To facilitate **scientific planning** and provide the basis for a unified advance of the whole interdependent state complex, socialism requires an accumulation of capital, equal, at least, to that of advanced capitalism. It requires adequate stocks and reserves to respond to circumstances like poor harvests, changes in market conditions, seasonal variations in demand etc.

5.5.1 The law of Primitive Socialist Accumulation

Preobrazhensky saw PSA as distinct from capitalist and socialist accumulation. PSA refers to the state economy accumulating resources from the non-state economy. He saw this as the basic and central law governing the motion and processes in the Soviet economy in the 1920s. It determined the distribution of the means of production and labour power, and the quantity of surplus product made available for the expansion of socialist production through its conflict with the law of value (Preobrazhensky, 1965, pp. 84–85).

Where planning operates, regularity of causation is consciously organized and shaped by state actions. It fights for its existence and consolidation and takes the form of expanded socialist reproduction. This entails increasing the proportion of the economy in state hands, integrating more of the workforce around these means of production, raising the productivity of labour, and struggling to expand reproduction of the system by maximizing PSA.

This process is seen as ‘the whole aggregate of tendencies, both conscious and semi-conscious’ and is also ‘the economic necessity, the

compelling law of existence and development of the whole system, the constant pressure of which on the consciousness of the producers' collective of the State economy leads them again and again to repeat actions directed towards the attainment of optimum accumulation in a given situation.' (Preobrazhensky, 1965, p. 58)

Defining the optimum rate is a complex task; inadequate foresight and excessive acceleration can produce negative consequences e.g., a goods famine and private sector accumulation. The study of economic regularity in the struggle between planning and commodity economy pleads for a method of generalization.

5.5.2. Economic equilibrium in the USSR

When Preobrazhensky wrote *The New Economics* in the mid-1920s. It was to be part of a larger work designed to facilitate the concrete study of the Soviet economic system: a theoretical framework that could be filled with the real data. The premise for Preobrazhensky's model of primitive socialist economic reproduction was non-equivalent exchange - this assumes that different systems of ownership compete to regulate the economy during the transition to socialism - the law of value and the law of PSA.

Marx's model of pure capitalism studied reproduction of the means of production (department I) and means of consumption (department II). Preobrazhensky's model of reproduction under PSA includes petty production and capitalist production as sources of accumulation, and as a means to acquire sufficient elasticity to maintain equilibrium (Preobrazhensky, 1980, p. 36).

The following charts (figures 7, 8 & 9) present Preobrazhensky's model of expanded reproduction for the three sectors of the Soviet economy (Preobrazhensky, 1980, pp. 182-183).

Where the chart refers to C V and S (in upper case)

C =constant capital

V = Variable Capital

S= Surplus Value or Surplus Product

MP1 = production of means of production

MP2 = production of means of consumption

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Figure 8. Chart of reproduction of the capitalist sector in Preobrazhensky's schema

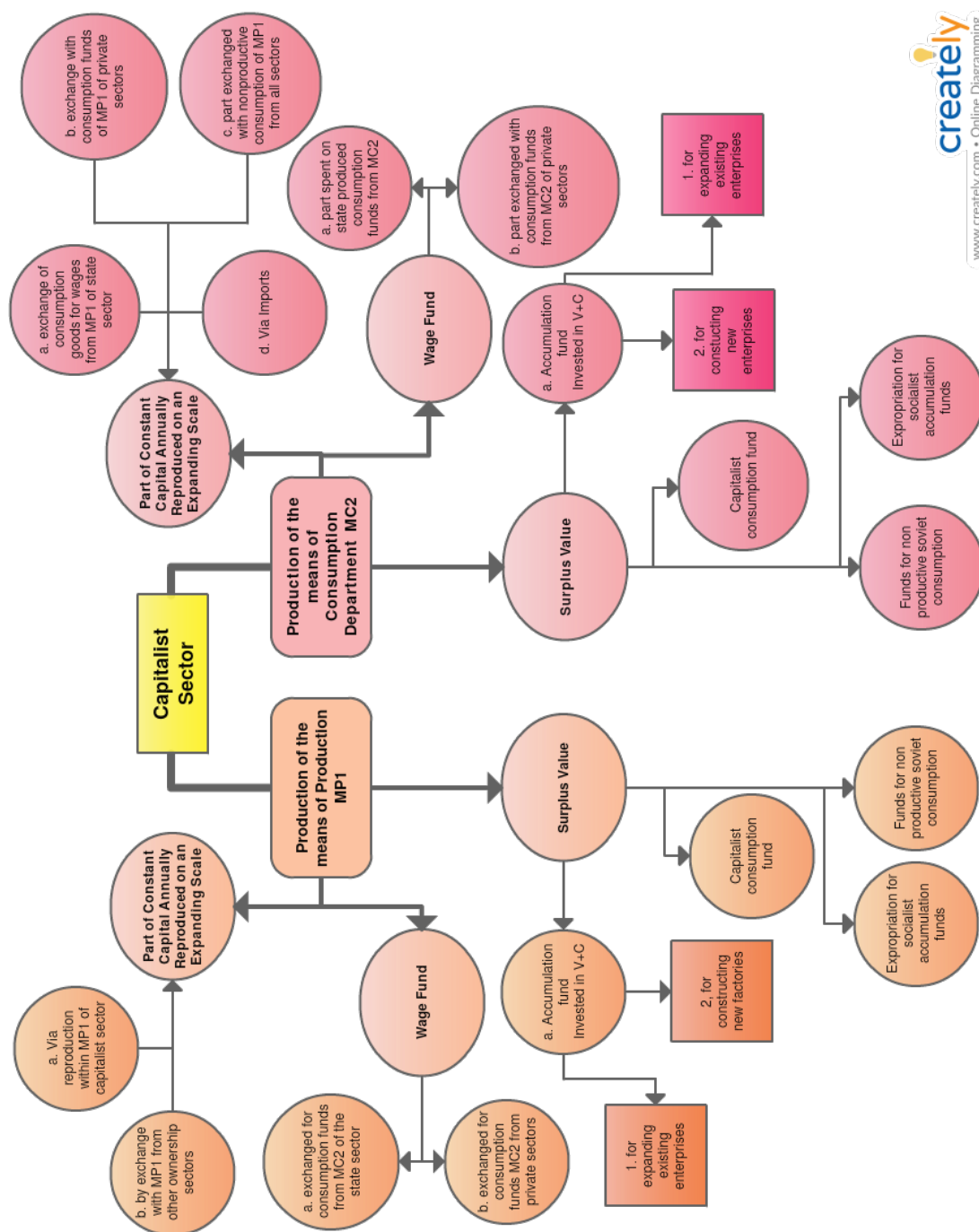
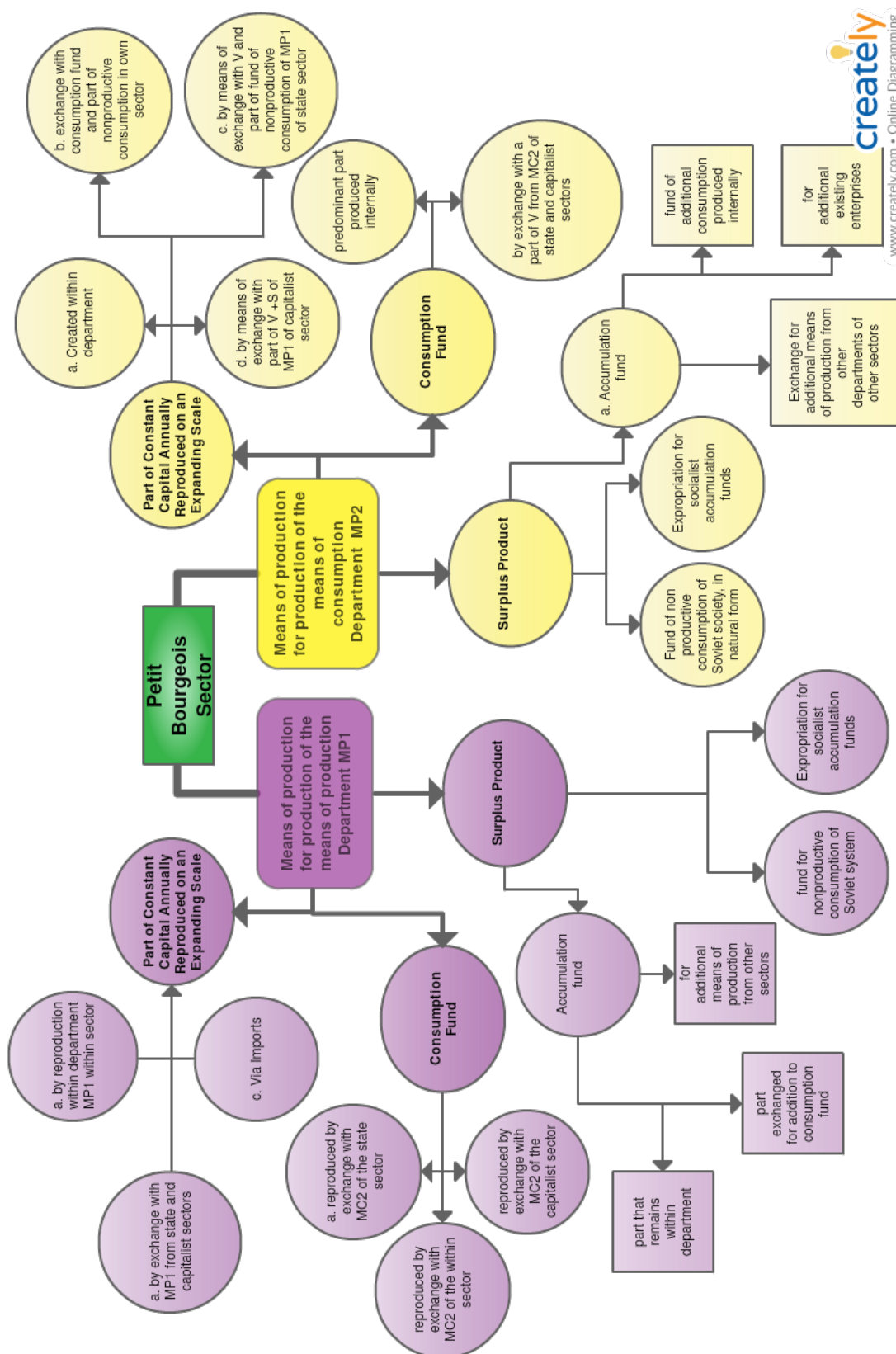


Figure 9. Chart of reproduction of the petit bourgeois sector in Preobrazhensky's schema



The three charts (figures 7, 8 and 9) above represent Preobrazhensky's sketch of economic reproduction in the Soviet system during the New Economic Policy. The charts divide the Soviet economy into three types of ownership: the state economy, the capitalist economy and the individual economy. Each of these is divided into two sectors: the production of the means of production and production of the means of consumption. This illustrates the spheres from which the state economy could accumulate resources during the era of primitive socialist accumulation.

5.5.3. Contradictions of development and equilibrium

Preobrazhensky identified the following contradictory foundations of development and equilibrium in the Soviet economy. Although some of these issues relate to specific problems of the Soviet Union in the 1920s, others relate to more general problems that would confront any developing socialist economy.

- Accumulation by the state is based on non-equivalent exchange and seeks to advance the productivity of labour and raise wages
- A rapid integration into the world market occurs in an external environment dominated by capitalism
- Accumulation from expanding industrial raw materials production takes place at the expense of peasant producers
- Accumulation from exports of consumption goods produced by the peasants, occurs while industrial prices only fall slowly
- Stimulation of peasant production for the market occurs whilst protecting weaker sectors of the peasantry
- Production rationalization and price reduction takes place whilst seeking to control unemployment.

In the late 1920s, Preobrazhensky feared that the scale, severity and acuteness of these contradictions reinforced the need for international assistance i.e. if a revolution occurred in an advanced capitalist country

like Germany, it was assumed that a socialist Germany would provide material and technical assistance to help the Soviet economy (Preobrazhensky, 1980, p. 230). This issue lay at the heart of the conflict between the opposing factions of the party led by Leon Trotsky and Stalin. Trotsky argued for the need for revolutions in other countries to stop the degeneration of the revolution and prevent a counter-revolution, Stalin argued that socialism could be built on an indigenous basis and, therefore, international policy should aim to neutralize potential enemies.

During the NEP, the capitalist sector was generally non-industrial and non-productive - exploiting opportunities provided by non-equivalent exchange. Private traders opportunistically exploited shortages or poor distribution. The main sphere of competition with state industry was light industry, where low capital costs and extreme exploitation predominated in the private sector. Wealthy peasants known as kulaks represented agrarian capitalism. The kulaks were hostile to the social system, which they blamed for restrictions on opportunities for enrichment. They engaged in strategies to accumulate at the expense of others. Their limited opportunities drove them to seek access to free markets by means of political opposition to the state.

'Here, the problem of economic equilibrium rests squarely on the problem of social equilibrium, that is, the relation of class forces for and against the Soviet system. Two systems of equilibrium are struggling for supremacy: on the one hand, equilibrium on a capitalist basis- which means participation in the world economy regulated by the law of value- by abolishing the Soviet system and suppressing the proletariat, and on the other hand, equilibrium on the basis of temporary non-equivalent exchange serving as the source of socialist reconstruction and *inevitably signifying the suppression of capitalist tendencies of development, particularly in agriculture.*' (Preobrazhensky, 1980, p. 179)

5.6. Studying a transitional state

This section provides an overview of the way that Preobrazhensky applied his theory of PSA to study the Soviet Union during the NEP. I focus on those concepts and policy proposals which are similar to core concepts and policies that have been pursued in China during the reform era.

Preobrazhensky's study of the dynamics of the New Economic Policy was concerned with the process of decay and disappearance of capitalist production relations. He attempted to identify which elements of Marx's political economy were verified by experience and which needed to be amended. Studying the NEP, which was a system driven simultaneously by contradictory laws, was complicated by the impurity of both forms. As planning under PSA operates in conflict with the law of value, the interplay of these contradictions had to be unravelled.

The state guided the economy, the government, and international policy, in opposition to the domestic private sector, and world capitalism. The relation of forces shapes the character and dynamics of the law of PSA. Studying the law means identifying its pure form and explaining its limits within this mixed environment.

State policy during the NEP was composed of responses to difficulties as well as anticipatory actions. This added complexity to studying the system, as many freely chosen policies resulted from resistance by the private economy.

'The conscious decisions of the regulatory organs of the State are dictated equally by the optimum of primitive socialist accumulation and by the need to curtail this optimum as a result of resistance of private economy and the classes which represent it. To separate the optimum in its pure form from the actual policy, which is forced to retreat from this optimum, is a very difficult task. To fulfil this task we need a concrete analysis of the entire economic and political situation at each moment of

time, or at least in a definite period of economic development.’
(Preobrazhensky, 1965, pp. 62–63)

For Preobrazhensky, the theoretical method used to study the Soviet system during the NEP had to be transitional between political economy and social technology. In other words the regularities of a mixed “commodity-socialist economy” were the object of study i.e., how collective production is shaped when linked to the private sector; and how the private sector behaves, in itself, and in relation to the state economy, when it is restrained and channelled by planning. As the commanding heights of the economy were in state hands, this created new processes in the state and private sector. Preobrazhensky saw his task as distinguishing, in pure form, the tendencies of the two conflicting principles and their methods of utilizing materials and labour (Preobrazhensky, 1965, p. 63).

Preobrazhensky defined PSA as the conscious and semi-spontaneous tendencies towards the collectivist organization of labour driven by necessity. The organization of the productive forces, defensive power, and the determination of material proportions to optimize expanded socialist reproduction are shaped in conflict with the law of value, and by pressures from the non-socialist economy.

This means that wage levels, price policy, trade policies and rules, tariffs, credits, import planning, government budgets etc., and the quantity of surplus extracted from the private sector, are all subordinate to the law of PSA (Preobrazhensky, 1965, p. 146).

The law of PSA extends into the private sphere as an alien force, but the law of value also penetrates into the state economy (Preobrazhensky, 1965, pp. 137–138). This produces ‘the coexistence of two systems of economy which are different and by their very natures antagonistic, with different regulatory mechanisms, this economy, must inevitably be the arena not only of struggle but also of a certain equilibrium, and so, in

practice, of a certain coexistence of two different economic laws.’
(Preobrazhensky, 1965, p. 138)

This equilibrium is has two main features:

1. The non-equivalent exchange of PSA, conflicts with the law of value until capitalist technique is surpassed. And the collective economy is in constant and unstable struggle against national and international capitalism and the world law of value.
2. Planning must proportionately balance expanded reproduction to prevent the law of value from breaking into and disrupting the process.

The import of means of production can alleviate internal disproportions and industrial backwardness. Such imports can be paid for by exports, purchased by the state from the peasantry. Close links to the world economy based on specific national characteristics, can help equip the means of production and finance raw material supplies. Planned imports of means of production become ‘an automatic regulator of the entire process of expanded reproduction’ (Preobrazhensky, 1965, pp. 197–203).

PSA and the law of value produce a unity in their outcomes, but their clash of forces reflects an underlying and fundamental antagonism between social systems and classes fighting for supremacy and for methods of regulation that correspond to their pure form.

Preobrazhensky thought that if the law of value became the sole regulator, the state economy would disintegrate. This would entail reorganizing the economy to facilitate the spontaneous reproduction of commodity-capitalist relations. In this scenario he predicted the abolition of the foreign trade monopoly, a reduction in the rate of industrialization, the closure of unprofitable enterprises, and the redistribution of productive forces between light and heavy industry, and town and country (Preobrazhensky, 1965, p. 64).

If the state sector strengthens – in defiance of the law of value – this indicates that another law, suppresses, modifies and amends the law of value. Knowledge of the existence of two conflicting laws facilitates the study and assessment of their relative weight, and an understanding of the characteristics of this constellation (Preobrazhensky, 1965, pp. 138–139).

If the state sector pursued an optimal development scenario supported by international socialist change, then, planning would dominate, guide, and organize the economy. The proportions of the economy invested in the means of production, its distribution, and the use of labour, would differ substantially, both from reality, and to the capitalist alternative. Thus, the battle for the existence and development of the socialist sector reflects the impulse of its regulator to reproduce itself on an expanded scale and to shape the world in its image (Preobrazhensky, 1965, pp. 64–65).

Expanded reproduction of the state economy means increased production overall. This enhances the relative weight of the state sector and rearranges economic forces guided by the needs of proportionality. PSA encompasses these processes, and ensures the transfer of resources from the private economy to the public. It determines the anticipated redistribution of resources of the future, based on the level of organization of the state economy. It organizes investment in capital and construction in anticipation of future proportions, and attempts to plan under the pressure of necessity, dictated to it as an external law. Its unique strength lies in its ability to gather and combine the productive forces of the state to implement plans corresponding to forecasts. This limits and excludes the law of value, which continues to dominate the unorganized economy. PSA dictates a proportional distribution of resources within the state sector, requiring preparatory accumulation. However, policy failures may generate crises that strengthen the capitalist sector both economically and politically (Preobrazhensky, 1965, pp. 66–68).

Under capitalism the driving force of production is profit and its regulator is the law of value. Consumer needs are met by this mechanism and workers buy consumer goods out of their wages. The state economy must meet the social demands of its era, reflected in consumer demand on the one side, and an expanding rate of accumulation, requiring the restriction of consumption, on the other; 'expanded reproduction in the socialist sector means automatic, quantitatively-increasing reproduction of socialist production-relations, together with the corresponding proportions every year in the distribution of productive forces.' (Preobrazhensky, 1965, pp. 72–73)

The conversion of the state economy into a single trust composed of giant interlinked corporations, and improvements in technique and productivity, change the form of value and its relation to labour-expenditure. These factors help to elevate the technical level of state industry (Preobrazhensky, 1965, p. 74).

Preobrazhensky argued that as the law of value is systemically linked to private ownership of the means of production, therefore, unless public ownership of the commanding heights was merely a formal appearance, it was planned regulation that established proportionality in the Soviet economy, with the law of value making corrections to it. So, non-capitalist regulation produces its own objective economic needs and proportionality in a struggle against the law of value and its method of regulation on the basis of labour expenditure. So PSA 'will always be the resultant of a struggle – though the direction in which the law of value and the law of socialist accumulation act may sometimes coincide in particular cases in real life.' (Preobrazhensky, 1965, p. 75)

Preobrazhensky tried to establish how the new economic system would oust, subordinate, and eventually eliminate old economic forms, which imposed their laws of resistance. A study of this process was complicated by the weakness of the new form of economy. The socio-economic influence of petty production and the peasantry also meant that an economic struggle would ensue between capitalist and socialist

accumulation from this large intermediate 'nutrient base' (Preobrazhensky, 1965, pp. 77–78).

As large-scale industry was nationalized, the law of value was undermined by state monopoly. However, petty peasant production exerted huge counter-pressure to develop on the basis of the law of value.

These conflicts between market spontaneity and the state economy, 'explain the predominant type of all the upheavals and depressions which we have suffered, are suffering and will go on suffering in our economy; together, of course, with those complications that are bound to arise from the connection between our economy and the world market.' (Preobrazhensky, 1965, p. 162)

Ties to the world market and the proportions of the economy in state and private hands determined the rate of accumulation. For Preobrazhensky over-accumulation of fixed capital was impossible during the NEP, as decades of development lay ahead, and private sector domestic demand would also rise (Preobrazhensky, 1980, p. 196).

5.7. Methods of PSA in the NEP

During the NEP Preobrazhensky applied his theory of PSA to concrete reality. His policy proposals were designed to rapidly accumulate state capital so that socialist economics could establish its dominance and reveal its advantages. He suggested a wide range of measures to secure PSA: taxes on profits; policies on banking, credit and foreign loans, extracting rent, exploiting inter-sectoral trade and the world market; controlling foreign trade and prices; and exploiting the power of state monopolies.

The capitalist credit system had been progressive relative to the unorganized markets of simple commodity production. State lending and credit in the NEP helped to structure the peasant economy. And the

credit system reflected the relation of forces between sectors of the economy. However, within the state sector, money acted as a means of accounting and calculation, rather than a key instrument for achieving spontaneous equilibrium in production. The system of planning, accounting and control, stemmed organically from socialization of the commanding heights of the economy and generated different results than capitalist banking (Preobrazhensky, 1965, pp. 209–217). It was Preobrazhensky's view that the viability of state banks should be judged by the total societal benefit of their credit and lending policies. Indeed, he explores the idea that judicious loans to the private sector could become a tool to channel, influence and structure investments to meet state objectives (Preobrazhensky, 1965, pp. 96–98).

Foreign loans, for Preobrazhensky, 'constitute a synthesis of capitalist and socialist accumulation'. They could accelerate socialist accumulation and technology transfer and create employment. Such loans should be evaluated by advantages to the system as a whole (Preobrazhensky, 1965, pp. 134–135). However, if basic branches of the state economy needed to grant concessions to secure investment, foreign capital would penetrate and weaken the system. So too, if the working conditions in such capitalist enterprises were superior to those in state enterprises. Nevertheless, he wrote: 'When the socialist form is consolidated economically and technically, concessions will no longer be a danger to us.' (Preobrazhensky, 1965, p. 136)

As land was nationalized, rent played a fundamentally different role to that under capitalism. Rent paid by state enterprises simply redistributed resources. The state appropriated rent from foreign concessions, mixed concessions, private farms, and wealthy 'kulak' peasants, who exploited wage-labour on public lands. These rents constituted a transfer to the socialist accumulation fund. Rent-tax on non-exploiting peasants and on the personal labour of kulaks, alienated surplus product from non-capitalist agriculture, but excluded the poorest peasants (Preobrazhensky, 1965, pp. 202–208).

Preobrazhensky proposed that trade policies between economic sectors be organized on the basis of the expedient requirements of PSA, such as reducing costs, edging out intermediaries and taxing private profits. He hoped that private capital could be coaxed into investing in sectors that benefit society (Preobrazhensky, 1965, pp. 99–103). Thus, if private capital were ousted from trading state products this ‘would undoubtedly intensify the process of transition of private capital into private industry, a process, generally speaking, which is economically advantageous and harmless provided there is a rapid growth in the state economy.’ (Preobrazhensky, 1965, p. 103)

Preobrazhensky saw the state monopoly of foreign trade, or “socialist protectionism” as a cornerstone of primitive socialist accumulation. It protected against the world law of value and helped to regulate the whole economy. As exports of agricultural commodities grew and trade increased, the foreign trade monopoly secured PSA from the surplus profits of these exports. Indeed, even loss-making foreign sales by the state could fund equipment purchases of benefit to the whole economy (Preobrazhensky, 1965, pp. 104–108). The world law of value influences the distribution of labour, e.g., where costs and benefits determine if resources should be reallocated. State planning should exploit opportunities provided by the world division of labour (Preobrazhensky, 1965, pp. 164–166).

If the state made losses in its exchange with the private sector this would undermine large-scale state production and result in the sale of fixed capital and/or proletarian labour power at bargain prices. If neither system of ownership exploits the other, this would indicate that there is no fundamental clash of economic interests; and thus equilibrium can be maintained indefinitely.

However, Preobrazhensky regarded capitalism as a system that always seeks to erode the socialist form, which, in turn, expands at the expense of the private economy. He advocated that the price policy of monopoly state entities should exploit the private economy but warned that where

private competitors participated in the same markets, state price policies could end up assisting private accumulation. And, as state price policies can adversely affect peasants and workers, he proposed measures to help counteract this, e.g. by means of credit and wages policy (Preobrazhensky, 1965, pp. 108–112).

Accumulation based on expanded reproduction of the state economy exploits the working class, i.e. it pays less than the value they produce. In War Communism production to meet emergency needs cost more than it produced, but losses had to be weighed against the alternative of zero production (Preobrazhensky, 1965, pp. 116–117). Preobrazhensky wrote: 'socialist production has to pass through a fairly long period of accumulation of material resources, during which the individual enterprise of the state economy will inevitably be not superior but inferior to, economically not stronger but weaker than, a contemporary capitalist enterprise in an advanced capitalist country.' (Preobrazhensky, 1965, p. 120)

Under PSA, reconstruction required rapid accumulation, technical development, and the rational geographical distribution of industry. The more developed the initial economic base, the more surplus product the workers provide - so resources from pre-socialist production would be less important (Preobrazhensky, 1965, pp. 120–121).

The struggle of the state against private economy focuses on the accumulation of material resources and the redistribution of labour power. The victory of capitalism over petty bourgeois and natural economy is the product of competition, technique and efficiency. The competitive superiority of socialist production does not pertain in relation to world capitalism. Free competition would disintegrate and destroy a socialist economy unless it had almost universal superiority in productive technique and efficiency, as the products of state industry will be more expensive and of inferior quality to that of advanced foreign capitalist enterprises (Preobrazhensky, 1965, pp. 124–127).

‘Inside the country private industry is weaker only because it is not allowed equal conditions for struggle. The state has held from the start the largest and technically most advanced enterprises. Furthermore, and this is most important, private industry is in every other respect placed in a less advantageous position than state industry.’ (Preobrazhensky, 1965, p. 128)

Although state enterprises may resemble private enterprises, the unified totality of state power produces its own necessities and demands. Its methods of gathering forces, and of finding and exploiting advantages, derive from the cooperative potential of “great economic masses”. Preobrazhensky forecast that the field of free competition with private enterprise would gradually contract, although competition could and should be used to help discipline and rationalize state enterprises. Ultimately, socialism would conquer by suppressing competition with pre-socialist economic forms and by unifying state power with the state economy (Preobrazhensky, 1965, pp. 129–132).

5.7.1. State relations to petty production and cooperation

Preobrazhensky wrote: ‘Capitalism by creating a single organism based on exchange provides the basis for a transfer to direct relations between state and petty production.’ (Preobrazhensky, 1965, pp. 131–132)

Capitalism conquered society with people disciplined in its forms of stimuli, but socialist habits and culture had to be created within the new system. In 1923 Lenin wrote that cooperation under the economic and political dominance of the working class could realize many of the dreams of utopian cooperative advocates of the past. He simultaneously spoke of the need for a prolonged revolution in the cultural and educational level of the peasants, and for the remodelling of society to peacefully transform peasant production into cooperative forms. He saw this as dependent on material development and education, predicting it would take a minimum of one or two decades, or “an entire historical epoch”, to attain the cultural preconditions for this.¹²

Preobrazhensky believed that cooperatives linked to large-scale state production could influence the character of petty production and exchange, but private agriculture tends to expand faster than state or collective forms. 'If the development of socialist relations in our economy, which have their basis in industry, were to stop or to be very much slowed down, and capitalist relations began to grow faster, then regardless of their social structure, the cooperatives would either break up at once, or else the majority of them would desert their positions as rear-guard of the state economy, in order to go over to the side of capitalism.' (Preobrazhensky, 1965, p. 220)

'The balance can be changed not by some socialist miracles on the territory of petty peasant production, taken by itself, but only by a more profound influence of large-scale urban industry on peasant farming.' (Preobrazhensky, 1965, p. p.222) Technology and industrial products from the state could be used to encourage socialization of agricultural production, but the tempo of industrial development at the socialist core of the economy would be decisive in determining the outcome.

During the NEP, commodity production - making goods for exchange on the market - dominated private, state-private, and to a considerable extent, state-state relations. This could be positive, if increasing urban-rural commodity exchange assisted rapid state industrialization and improved organizational capabilities. Monopoly capitalism gained dominance over capitalism based on commodity production, and this laid the foundation for socialism, which would increase the degree of monopolization, undermine "free competition" and create, 'state monopoly in all large-scale and medium industry, transport, the credit system, and wholesale (and in part retail) trade, a state monopoly which surrounds itself with a powerful cooperative network.' (Preobrazhensky, 1965, p. 141)

However, where the law of value is partially effective, and the law of planning fails to create its own proportional relations of development, a

crisis may undermine state planning and enrich private capital. During harvest failures, imports can ameliorate shortages. However, declining prices would signal the need to purchase grain and expand exports. The exchange of consumer goods amongst peasants and artisans was the least regulated sphere of the economy. Peasants purchased most of the grain, food, and seed produced, but poor peasants often paid for this by working for wealthier peasants. So the law of value reigned supreme in market exchanges between peasants (Preobrazhensky, 1965, pp. 180–182).

5.7.2. Surplus value and surplus product

Preobrazhensky believed that surplus product takes the form of surplus value when the product created by the labour of exploited classes becomes a commodity. The product is only made in order to extract surplus value from the producer. The existence of free labour constitutes the final prerequisite for a transition to capitalist production (Preobrazhensky, 1965, p. 186). The realm of surplus value expanded as commodity production became capitalist production. However, in the USSR, Preobrazhensky observed the opposite process, a decline of surplus value, as socialist forms grew. The commodity was being transformed into the product, starting in state production of the means of production. Capital intensification extends the influence of production of the means of production, improving the quality and reducing the price of consumer goods.

Preobrazhensky concluded that 'the development of the productive forces must inevitably mean an increase in the relative weight of the production of the means of production, and this increase quite automatically intensifies the tendency for commodity production to disappear in the state economy and in this way undermines the category of surplus value.' (Preobrazhensky, 1965, p. 187)

State industry produced monopolistically for the market and the state. In the latter, market relations were more apparent than real, as competition

was undermined or even abolished. With advances in rural productive forces, Preobrazhensky envisaged increasing peasant production for the market. But as state productive forces increase, and state planning and organization improve, so state commodity-production would decline, corresponding to a decline in the category of surplus value (Preobrazhensky, 1965, p. 187).

5.7.3. Profit in the state economy

Preobrazhensky emphasized the role that the equalization of the rate of profit plays in distributing productive forces under capitalism. Capitalist firms face a number of unknown factors in relation to orders, sales, prices, markets, and profits. Equilibrium is established by changes in the rate of profit that attract or repel investment. The proportions invested in constant and variable capital differ in various entities and sectors. Enterprises with a variable organic composition of capital are all subject to equalization in the rate of profit.

Soviet state enterprises planned production in relation to planned demand, with greater fluctuations occurring where connections extended to non-state sectors. Input prices were either known - as state entities supplied them as part of a plan - or influenced, and contained. Wages were collectively agreed and could be planned for. Planned decision-making in the state economy altered the nature of profit, and thus the influence of the rate of profit.

Production based on standardized calculations undermines the regulatory role of prices and profits in the distribution of the productive forces, which are governed by general planning instead. The rate of socialist accumulation is regulated by planned inputs and sales. Profit ceases to be the source of accumulation or regulation (based on the law of value), determining the distribution of the productive forces (Preobrazhensky, 1965, pp. 196–199).

Under capitalism surplus destined for new investment flows into shares, which act as a spontaneous means of creating and distributing capital.

Although the Soviet economy also issued shares for joint-stock companies, the content differed from the capitalist form. State enterprises or institutions bought shares in each other. The state banking system was the primary means of distributing capital alongside the state budget (Preobrazhensky, 1965, pp. 199–200).

The basic mechanism for distributing new capital was the state banking system and the state budget. 'This distribution cannot be otherwise than planned, because it is completely absurd to suppose that the process of expanded reproduction of state industry and transport, all new construction, etc., can proceed in a planned way in the sphere of fulfilment of production programmes and yet can be unplanned, relying on some process of self-activity and spontaneity within the state economy, when it is a question of collecting resources for expanding reproduction.' (Preobrazhensky, 1965, p. 200) However, Preobrazhensky noted the underdeveloped state of organizational forms designed to raise resources for expanded reproduction. These are forms that he says are inherent to the state economy and should correspond to a specific stage of primitive socialist accumulation.

PSA in the NEP also developed spontaneously, in the sense that annual accumulation was not determined in advance using conscious and planned prices. Prices were developed by adding together the costs, rather than by working out the accumulation required and sharing this burden between various spheres of production.

Under capitalism competition regulates the economy. The equalization of profit shapes the distribution of labour despite differences in the organic composition of capital and the quantity of surplus value that the invested capital produces. The law of prices of production facilitates reproduction under capitalism. Capitalist accumulation funds combine the total surplus acquired by capital from labour. This is distributed amongst capitalist enterprises according to the law of profit equalization.

Profits of Soviet enterprises weren't divided into capitalist consumption and accumulation funds - there were only accumulation funds. However, a proportion was transferred to central state finances. The funds needed were worked out in advance as part of a production plan, and budgets and prices were adjusted to try to meet these plans. The accumulation fund was derived from price policy, and encompassed the entire state economy. Its component parts provided these funds from profits, which were more unequally distributed than under capitalism. Price policy and profits were designed to secure state accumulation (Preobrazhensky, 1965, pp. 200–202).

5.7.4. Labour-power as a commodity

Preobrazhensky described a transitional condition where:

- The private economy employed more people than the state¹³
- The reproduction of labour power also reproduced the commodity economy
- Consumer purchases came mostly from the private economy
- The state economy regulated the total labour fund by means of PSA, but gradations in wage scales were regulated by supply and demand.
- The wages fund related to the demands of planned accumulation not to fluctuations in the labour market; thus wages rose simultaneously with a labour surplus. There was a divorce between the wages fund and the law of value.

Preobrazhensky explained that capitalist forms, particularly in small and medium sized enterprises, exploited the workers, the staff, and the owners. The hours and intensity of their work defied socialist legislation. In trade, self-exploitation by owners played a significant role. So it was hard to envisage how socialist means could compete on unit costs of circulation. In this respect, protection of labour was a disadvantage vis-à-vis capitalist trading (Preobrazhensky, 1965, p. 133).

Primitive capitalist accumulation ruthlessly exploits labour, but is later constrained by the relation of forces. However, socialism restricts the exploitation of labour. The state economy produces for the consumption of the producers through the market exchange of commodities. The regulation of wages during PSA is not governed by supply and demand fluctuating around value, or by labour struggle, which is replaced by workers' self-restraint. Enthusiasm may temporarily boost production, but labour laws, regulations, social security and protection are more advanced than in comparative capitalist countries (Preobrazhensky, 1965, pp. 122–123).

Under the NEP the distribution of the wages fund remained bourgeois and was adapted to legacy forms and bourgeois incentives. Piecework was commonplace, but technical development began to restrict its operation. It was envisaged that individual and collective wages would merge and include provision by social institutions, crèches, clubs etc. Preobrazhensky used the term surplus product to characterize the fund acquired by state industry after satisfying workers' consumer needs. This refers to the state economy, where new production relations were 'coming into being'. The reality combined elements of surplus value, surplus product and collective expanded reproduction (Preobrazhensky, 1965, pp. 190–195).

PSA integrates the planned and spontaneous processes towards rapid expansion of the state sector. The law restricts wages in order to accumulate state investment funds. Therefore it slows down the tempo at which wages are changed into consumer rations. 'The tendency to overcome the category of wages, that is, the tendency to intensify the socialist quality of production-relations, comes into contradiction with the tendency to quantitative extension of the territory of the state economy and its production-relations in their present form, that is, production-relations at an extremely low stage of development in their socialist character.' (Preobrazhensky, 1965, pp. 195–196)

For Preobrazhensky the development of socialist forces of production was simultaneously understood as the formation and expansion of the working class in itself and for itself, i.e. of its creation as a productive class, and of its consciousness and its capacity to assume command and control over the work process, and the state - roles that the Soviet bureaucracy had already usurped. Preobrazhensky saw the role of the party as that of the 'guardian of the proletariat's interests until the latter had acquired the numerical strength and the political sophistication to manage its own affairs.' (Filtzer, 1976, p. 36)

Preobrazhensky took the view that democratic control by the workers, rather than bureaucratic administration was an essential component of socialist development. As with Trotsky and the Left Opposition, he believed these contradictions, imposed by backwardness, could be ameliorated or resolved only with the support of revolutionary change in the advanced countries.

As the working class remained a minority class with a low cultural level, it was incapable of assuming control over the administration of the economy and society. The factories were organised on capitalist principles, and non-proletarian specialists undertook the managerial and technical roles. This contributed to the formation and reproduction of a privileged bureaucratic stratum, which organized the process of industrialization (Filtzer, 1976, pp. 42–43).

And as Filtzer notes: 'Within the conflict between the law of value and the law of primitive accumulation there stood not just the class conflict of the proletariat with capitalist social groups, but also the nascent conflict between the proletariat and the bureaucracy.' (Filtzer, 1976, p. 45)

However, 'the bureaucracy was unable to appropriate power and control other than through property relations that had survived with the revolution and on the basis of adopting "Marxism" as its legitimating ideology.' (Filtzer, 1976, p. 46)

5.8. Ten propositions from Preobrazhensky that can help to explain China's system

I believe Preobrazhensky's theory can also shed light on the way that China's social and property relations have been produced and reproduced in the reform era. In this thesis I do not attempt to apply Preobrazhensky's framework in detail to the study of China. However, I find that many of the features of China's system in the reform era bear a close resemblance to the analysis and theory that Preobrazhensky worked out in the 1920s. The following is a list of ten propositions from Preobrazhensky that can help to explain the dynamics of China's system.

1. During the period of PSA, capitalist and state ownership, and their corresponding laws, are both effective. The collective economy operates in conflict with the capitalist economy. These contradictory ownership forms press to organize the economy in their own image, but there are also periods when they push in the same direction.
2. State dominance of the commanding heights is essential for the survival of the system. Planning policy has to secure expanded reproduction, or else the law of value will disrupt the process and become dominant.
3. Combining the strength of giant interlinked enterprises and raising their technical level secures state sector dominance. Expanded reproduction of the state sector is generated by its own internal impulses and acts to structure the overall economy. If the state economy advances, this is evidence that the dominant law governing the economy is planning based on PSA. Although, state enterprises may superficially resemble private companies, the cooperative potential of these great economic masses produces its own necessities and demands. Trade policies between the state sector, and the capitalist, and individual economy, should be contingent on policy objectives, e.g., supporting specific industries squeezing out competitors, reducing costs etc.
4. The unique strength of the state economy under PSA lies in its ability to gather and combine economic resources to implement plans. The state sector must act to contain the influence of the law of value. PSA must ensure that the public economy develops proportionately and this

requires accumulated reserves. Rents paid to the state constitute part of the socialist accumulation fund.

5. Economic planning should exploit the opportunities that close integration with the world economy provides. National comparative advantages should be designed to secure raw materials and advance the technical level of the means of production. Imports are an essential means to achieve technical progress. Competition with the private sector can help to discipline state enterprises.
6. The economic geography of the country can be rationally planned and developed by means of PSA. The gigantesque scale of the investment in fixed capital required to modernize the economy makes a mockery of talk about the over-accumulation of fixed capital. Under socialism planned investment undermines the dominant role of profits.
7. The success of state banks should be assessed by the degree to which society benefits. State banks should judiciously lend to private enterprises in order to channel their investments and assist state objectives. Foreign loans and concessions can be advantageous for technical development, provided the state economy is consolidated and secure. The organization of foreign trade needs to ensure that export revenues are beneficially used. Free global competition would undermine the state economy unless it is more efficient than world capitalism.
8. In a country with a large peasantry, competition between capitalist and socialist forces, takes place over the surplus produced by this 'nutrient base'. The socialization of agriculture should not be prematurely imposed, as its progress depends on state-led industrial development.
9. The rate of profit shapes the distribution of the productive forces under capitalism. Individual private capitalist enterprises are inevitably more 'profitable' than state enterprises. If the private economy is treated on equal terms with the state economy this will undermine and ultimately destroy it. If capitalist relations gain the upper hand the state economy will begin to disintegrate and will be dramatically restructured in a way that undermines state planning.

10. Over time the spheres where the state and private sector operate in competition with each other should decline, whilst maintaining and expanding the dominance of the public sector.

5.9. Conclusion

Preobrazhensky regarded Primitive Socialist Accumulation as the totality of measures that a socialist state can take to acquire resources from the pre-socialist sectors of the economy to help the socialist sectors to reach the productivity of labour of advanced capitalism. Capitalist primitive accumulation occurred prior to the overthrow of feudalism but PSA would be a general law for development of a socialist economy, unless the socialist revolution takes power in an advanced capitalist country.

The specific conditions in the Soviet Union during the NEP demanded large-scale investment to reequip Soviet Industry at a new technical level. For this reason, the main source of the required accumulation funds would come from agriculture. Even then it was envisaged that differentiation between rich, middle, and poor peasants, would ensure that the exploitation of the peasants would be less arduous for most peasants than the burdens of pre-revolutionary forms of exploitation. As Preobrazhensky explains: 'If capitalism took, say, 20 roubles from 100 roubles of peasant income, why cannot the socialist state take say 30 roubles from an income of 300? All the more since, through the channels of long-term credit, equally beneficial for the success of accumulation in industry and in agriculture, we shall return part of these resources to the peasant economy in the form of capital.' (Preobrazhensky, 1965, pp. 254–255)

In the Soviet Industrialization Debate, Preobrazhensky regarded the expansion of the relative strength of the workers and the state sector of the economy as a decisive main benchmark of success. His theory was that the law of value, based on market relations, had to be countered, contained, channeled, and subordinated to the socialist objectives of the state economy. This was why state planning had to be elevated in

importance but also had to be designed on the basis of the optimal accumulation. This optimal could be based on short, medium and long-term objectives.

When planning won the day in the late 1920s this appeared to represent a confirmation of the arguments of the opposition. The policies that were adopted: the introduction of five-year plans; a concentration on heavy industry; and the isolation of the kulaks and wealthy NEP traders, echoed the demands of Preobrazhensky and the Left Opposition made in the years before 1928.

However, the way these policies were enforced represented the expression of the rising power of the bureaucratic apparatus led by Stalin. Whereas Preobrazhensky suggested multiple ways to acquire resources from the private economy whilst coexisting with it, Stalin's methods, representing bureaucratic solutions, employed crude means based on the large-scale use of force.

Preobrazhensky saw the conflicts that emerge in a mixed economy under PSA as inevitable expressions of conflict between the state and private economy. He believed that such upheavals would continue to break out, as they expressed the contradictions between social classes nationally, and internationally.

As with the period after the consolidation of Stalin's rule in the late 1920s and early 1930s in the Soviet Union, after 1949, China's leaders also had to design policies that provided the means to modernize and industrialize. In China bureaucratic pressures also emerged spontaneously as a result of social pressure to develop the economy. This background closely corresponds to Kornai's explanation of the pressures that automatically generated the dynamics of forced growth.

However, rather than locate periods of greater market influence in China as expressions of trends to abandon state planning and control, I believe the greater role for the market and the private economy in the reform era,

created a terrain in which a richer variety of sources could be exploited for the purposes of primitive socialist accumulation - albeit in a bureaucratic form that automatically generates pressure to adopt forced growth. This pattern has held true in periods of centralization and decentralization.

Ultimately, one can speak of primitive socialist accumulation as a catch all term for the whole epoch. And it can include all measures that acquire resources for the state sector from the private sector in a socialist economy. However, for Preobrazhensky's PSA was explicitly *not a policy of universal bureaucratic expropriation, as the accumulation process is closed off by universal nationalization*. It is my view that the economic structure in China since 1978 bears a closer resemblance to an environment in which PSA can bear bountiful fruit than those systems that Kornai defines as classical socialism.

Kornai's theory is that reform socialism is a system that is by definition, automatically dysfunctional, incoherent, and doomed. This is clearly incorrect, if China's system does indeed correspond to his model as I have argued in chapter 3. The vastly expanded terrain for accumulation from the private economy that China's reforms permitted, simultaneously represents a vast extension of the terrain for PSA, even though this is realized in a bureaucratic form. In chapter 6 we look at how China's modern working class was formed.

¹ In 2017, just as I was completing this thesis, two Danish Sinologists, Brødsgaard, and Rutten published the only English language work that considers China's system in depth with explicit reference to Preobrazhensky (Brødsgaard, and Rutten, 2017). However, although I made very close study of this work, and attempted to find some way to incorporate aspect of its contents, I was reluctantly forced to conclude that this task would require a major work of critical analysis. This is because the central claim of the authors, that Preobrazhensky's theory of Primitive Socialist Accumulation was at the heart of all policy making in China since 1953, is very misleading. So, I felt obliged instead, to focus on explaining what Preobrazhensky actually did write, rather than engaging in a polemic that would revolve around refuting conclusions based on false assumptions.

² The term used by Marx for the capitalist process was *urprünglicher Akkumulation*. The English translation as primitive accumulation seemed to be appropriate, as it was illustrated by cruel and brutal methods such as the slave trade and the forcible dispossession of the peasants. However, translating *urprünglicher Akkumulation* as 'original accumulation' would corresponds more closely with the concept that Preobrazhensky developed. Nevertheless, despite this unfortunate translation the term primitive socialist accumulation is used throughout the English translation of *The New Economics*, so I will also use it throughout this chapter. The reader should bear in mind that I consider original or initial socialist accumulation to be a more appropriate term.

³ Preobrazhensky was expelled from the party, readmitted after capitulating to Stalin, but then changed his mind, and was expelled again. He was eventually executed in 1937.

⁴ A purely geographical frame is inadequate as it fails to account for Preobrazhensky's approach to differentiation within the peasantry.

⁵ Preobrazhensky equated state ownership in the USSR with socialist property.

⁶ Preobrazhensky's concept of exploitation deals with the extraction of surplus product from the peasantry and the private economy by means of unequal exchange, i.e., an exchange of products containing different quantities of labour time.

⁷ I believe this can also be said of premature or excessive state intervention, for example setting the tempo of industrialization too ambitiously or nationalizing productive assets before they are sufficiently developed.

⁸ Although, Marx correspondence with Vera Zasulich in 1881 supported the idea that ancient communal property forms in Russian agriculture, known as the Mir, might be combined with a revolutionary transformation of society to bypass capitalist industrialization and mechanize on the basis of collectivism.

<http://www.marxists.org/archive/marx/works/1881/03/zasulich1.htm>

⁹ <http://www.marxists.org/history/etol/document/ilo/1923-lo/ch03.htm> 11 Dec 1923

<http://www.marxists.org/history/etol/document/ilo/1923-lo/ch04.htm> 10 Jan 1924

<http://www.marxists.org/history/etol/document/ilo/1923-lo/ch05.htm> 16 Jan 1924

¹⁰ Trotsky, Zinoviev and Kamenev and other well-known Bolshevik leaders created the United Opposition in July 1926 to change party policy and fight against bureaucratism.

¹¹ Carr 1969 p.308

¹² See Lenin On Cooperation Jan 4 & 6, 1923

<http://www.marxists.org/archive/lenin/works/1923/jan/06.htm>

¹³ In 1927 only 12.6% of the labour force were employed by the state (Preobrazhensky, 1980, p. 229).

6. The working class in contemporary China

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6.1. Introduction

China's ruling Communist Party (CCP) claims to represent the working class and the peasants. But China is host to some of the world's largest capitalist factories, and has hundreds of billionaires and hundreds of millions of exploited workers. These contradictions lie at the heart of China's political economy.

This chapter studies the role of the working class in China's political economy. It is informed by the Marxist approach to class adopted by the prominent US sociologist Erik Olin Wright. It begins with an explanation of his concepts of class, the working class, and class conflict. Wright identifies two forms of working class power - *structural* and *associational*: (Wright, 2000b, p. 962) structural power derives from location within the economic system; and associational power stems from voluntary

combination and action. These two categories frame this review of the historical development of China's working class.

I provide an overview of the genesis of the CCP's administrative power structure and the working class between 1929-1949. This is followed by short summary of the processes, which created the working class between 1949-1981. This draws on influential studies by the Australian Sinologist Andrew Walder (1984, 1986). Comprehensive research on China's social structure, conducted by Lu et al (2012) for the Chinese Academy of Social Sciences, provides the material for my survey of the formation of the working class since 1979. Then, I consider the relationship between the working class and the trade unions, and examine a variety of displays of independent associational workers' power in the reform era. I examine the forms and appearances that workers' struggles adopt, and consider the relationship between social unrest, and Party and state power in China.

However, prior to this broad overview of the development of the working class, I will return to one of Kornai's key theories, the socialist propensity to generate the soft budget constraint, because I believe that the implicit role of the working class in this process deserves to be made explicit.

6.2. The working class and Kornai's soft budget constraint

The role of the working class in China's political economy is the subject of this chapter. Kornai's systems theory does not deal with the working class as a direct subject. Instead it mostly gauges the influence of the working class through its impact on the soft budget constraint. He characterizes capitalism as a system of surplus production and surplus labour, and socialism as a system a shortage of goods and labour. And, whereas capitalism is governed by hard budget constraints, socialism produces soft budget constraints. Under the soft budget constraint, pressure to maintain peaceful relations in state owned companies and wider society, finds expression in paternalistic bureaucratic behaviour towards the workers. This is particularly significant where Kornai

describes “self-management” trends in which workers discover that they can exert pressure on higher-level authorities to dismiss managers. This compels managers to try to contain and avert threats to stability by ‘representing’ the workers vis-à-vis higher authorities. This reinforces and reproduces soft budget constraints, as the fear of unrest encourages managers to expand investment in state enterprises and projects that are designed to contain unemployment and discontent (Kornai, 2007, pp. 461–470).

Kornai also says that under socialism labour shortage arises from the system’s innate characteristics and propensities (Kornai, 2014, p. 95). The appetite for investment is insatiable, as public sector entities operate under soft budget constraints, and investment is only tempered by the restrictions of bureaucratic allocation. However, in the early stages of socialist development, a transfer of agricultural labour to industry occurs. When this surplus labour is exhausted the rate of growth is hampered by labour shortages. In China, urban-rural demographic proportions were frozen for decades under the household registration system. The toleration of mass migration to the cities after 1978 and state urbanization plans to facilitate this, continues to generate a huge influx of labour from rural areas into the cities. This constitutes a fundamental distinction with the macro level environment that Kornai considered in *The Socialist System* (Kornai, 2007).

6.3. Marxism, class and the working class

Erik Olin Wright developed abstract Marxist definitions of class that are simultaneously consistent with empirically observable processes. At the highest level of abstraction is ownership of productive assets: control over these assets enables relations of class dominance and subordination to be reproduced. Exploitative class relations exist where property relations between people assign power over assets unequally and, as a consequence, social groups can enforce corresponding claims to live from the productive labour of others. The character of these claims on property and exploited labour define the specific historical form of

exploitation and its mode of operation. Antagonistic class relations reproduce both exploitation and mutual interdependence. The character of a social system is defined by: the qualities of the class structure; economic reproduction; the forms of distribution; and patterns of development (Chibber, 2009, pp. 355–356).

Marxist theory approaches class from three perspectives: as a relationship between people and assets that can be used to generate income; as a macro level concept to explain historical variations in the way that economic surplus is extracted; and as a normative explanation of the changes required to end exploitation and oppression (Wright, 2003, pp. 2–3). To emancipate humanity, Marxism advocates the transformation of social institutions and elaborates the historical conditions in which such changes can occur. The core of class conflict is class exploitation generated within production. Exploitation pertains when there is a causal interdependence between the material interests of the exploited and exploiter. This is based on excluding the exploited from access to productive resources, which enables the exploiters to appropriate the labour efforts of the exploited (Wright, 2003, pp. 7–8).

The Marxist concept of class is concerned with relations of dominance, in which exploitation denotes appropriation of the surplus product produced by subordinate classes.

The dominant class:

1. Consumes in excess of their productive input and defines income distribution.
2. Exercises disproportionate political power, shapes social change, and determines investments and social and cultural development (Wright, 1979, p. 15).

The concept of modes of production defines how surplus labour is appropriated depending on class position within the social economy. Ownership of the means of production generally determines the ability to shape the technical division of labour and to command authority over labourers (Wright, 1979, pp. 14–17).

For Marxists, the dominant mode of production defines the primary societal contradictions. It determines the character of class struggle as well as the nature of transformation that is possible as a result of such conflict. Marxists adopt a normative stance in supporting outcomes that, they believe, correspond to their socialist or communist vision of the future.

Marx identified the proletariat as wage labourers collectively employed in commodity production to generate surplus value. He believed that the objective condition of the proletariat compels it to promote social revolution, in which, it assumes the leadership of the working class and the majority of society. Proletarian organisational power is externally imposed by capitalist discipline. The concentration of production and urbanisation of life creates the conditions from which its consciousness stems. Its class combination is a form of latent or actual struggle. The proletariat clashes with capital over its claim to exclusive power derived from private property rights. This reflects the fundamental contradiction between private appropriation and social production. It is the social position, power, and organic demands of the proletariat, that enable it to create a socialist society (Draper, 1981, pp. 34–48).

Wright argues that the dominant paradigm in the 20th century characterisation of socialism was focused on the mode of production and the economic structure. Socialism entailed a system that negated production for profit maximization and market exchange.

‘Since the pivot concept of capitalism is the private ownership of the means of production, generally this has meant that socialism is understood as public ownership in one form or another, most typically through the institutional device of state ownership.’ (Wright, 2010, p. 72)

Wright developed a triangular power paradigm, which presents modern class conflict as revolving around a struggle for societal dominance between three loci of power, statist, economic, and associational. Complete state power would resemble a Stalinist tyranny. Complete

economic power would be a right-libertarian economic utopia - where money rules everything. And complete associational power would resemble Karl Marx's vision of the highest phase of communism - where the state is supposed to wither away.¹ His concept of *power is defined as the ability to achieve objectives*.

Statist power is defined as the institutional 'capacity to impose rules and regulate social relations over a territory, a capacity which depends on such things as information and communications infrastructure, the ideological commitments of citizens to obey rules and commands, the level of discipline of administrative officials, the practical effectiveness of the regulations to solve problems, as well as coercion.'²

This concept of statist power helps us to consider how the CCP's system of power was established between 1929 and 1949, and how it created the working class in a structural sense from 1949-1978 and thereafter.

6.3.1. The origin of the CCP's power before 1949

The CCP was founded in 1921 under the influence of the 1917 Russian Revolution. It rapidly became a party of the working class but was routed from the main urban areas in 1927 by Chiang Kai Shek's nationalist forces. Following this defeat the CCP's main constituency of support was the peasantry. Mao Zedong 'sinified' Marxism by grounding it in local (rural) historical conditions. The CCP and its People's Liberation Army developed the ability to lead peasant movements and sustain revolutionary bases for two decades: in diverse ecological and geographical terrain; and in villages of varied class composition and traditions (Rousset in Au et al., 2012, pp. 238–245).

The CCP came to power and established the People's Republic in Oct 1949. However, from 1929-1949, Communists held power in what were called the 'liberated areas'. They varied greatly in size, form and duration. At their peak, they ruled over tens of millions of people. The CCP constituted the commanding centre of a system of power and

administration, which could be rapidly created, exercised and abandoned. The party was a revolutionary organization conducting warfare. Land reform was selectively championed as a means to secure the support of peasant forces. The party was flexible in its approach and its roots were often tentative and transient. The need to anchor itself in local conditions led to alliances with all manner of social forces whose support was deemed expedient to securing, temporary or enduring, territorial hegemony, or to exploit tactical or strategic opportunities in military conflict.

Liu Bin Yan, a former reporter for the *People's Daily*, wrote about the formation of the state in the pre-Liberation era: 'The first order of business for the military was to gain an understanding of the situation in the new area and determine who were its potential enemies; to do this it was necessary to reorganize the people's lives and issue new government decrees. In as much as officials of the previous regime were not to be trusted, activists willing to work for the new regime came to the assistance of the military and the party, and the most loyal and competent among them were recommended or appointed by military or party officials as local officials... the Chinese party established a system of control over a nation of one billion people based upon its experiences in military control, in which a given area might be abandoned at any time. It is not a complex system: political loyalty to the party is the prime consideration in appointing an official, far more important than abilities or cultural level; the reinstatement, promotion or demotion of an individual is invariably determined by how an official higher up feels about him, rather than by his character, morals, abilities, or achievements or by how the masses feel about him. The bureaucrats' children often intermarry, establishing a blood relationship or what is called a kinship relationship. School ties and such things as the place of birth unite the bureaucracy together. If one man commits a crime, the network is mobilized to form a protective cloak around him; it is very effective. In 1957 Mao revealed that 'there were at the time 1.8 million officials throughout China.' There are now 27 million.' (Liu, 1989, p. 61)

In central China a significant proletarian cadre, composed of revolutionaries from Shanghai, fertilized the New Fourth Army, whose methods and territorial base diverged significantly from that of Mao's better known Eighth Route Army. Thus, for two decades in advance of 1949, the CCP created diverse forms of statist power involving a wide range of social forces and alliances. So, the origin of the CCP's administrative state system was 1929 not 1949. The specific characteristics of this form of state power and the social base that sustained it differed depending on the material environment and the tactical and strategic objectives being pursued (Benton, 1999, 1992).

6.4. Class and social strata in official ideology

The structures of state and economic power are based on social relations between different strata and classes in society. This system of social stratification is now the focus of investigation.

The official theory of class relations in China begins from the following arguments:

1. China is at the primary stage of socialism.
2. The working class is the leading class and the peasants are its allies.
3. The rule of the working class is reflected in the dominance of public ownership, the ideology of the party and state, and the rule of the CCP.
4. The rule of exploiting classes has been overthrown.

	Social strata	Percentage of working population
1	State and social administrators: party cadres with power over organisations and resources	2.3
2	Private entrepreneurs: employ others and invest for profit	1.3
3	Managers: high and mid-level managers in charge of departments and resources	2.6
4	Professional and technical staff in state agencies and institutions	6.3
5	Clerks engaged in routine administration	7
6	Individual micro-level business	7
7	Employees in commercial services	10.1
8	Industrial and construction workers	14.7
9	Agricultural labourers who work mainly or exclusively in on collective land	40.3
10	Urban and rural jobless, unemployed or semi-employed or disabled	5.9

Figure 10 above is based on a survey of 1% of the population of China carried out in 2005.³

The National Bureau of Statistics grades China's current class structure into 10 social strata. This is shown in the table above, which follows the method developed by Lu Xueyi (Lu, 2012), who is a keen advocate of strata based analysis defined by 'occupation... the possession of organizational authority, economic and cultural resource(s)' (Lu Xueyi cited in Goodman, 2014, p. 28).

Wang attempts (Wang, 2015) a comprehensive Marxist theoretical analysis of China's class relations by drawing on the CCP's present-day ideology. Central to his argument is the view, drawn from Mao Zedong, that there are contradictions that are antagonistic and others that are non-antagonistic. Wang says that the establishment of the People's Republic as a socialist state led by the CCP abolished exploitation and all fundamentally antagonistic class relations: a rather bold claim. Consequently, conflicts that emerge are conceptualized as non-antagonistic, i.e. they can be resolved within the system by good leadership. The struggle over the interests of various strata within classes is the form of antagonism that replaces class struggle and constitutes a 'contradiction among the people' (Wang, 2015, p. 176). Wang identifies the character of such interests by ownership of the means of production, roles in processes of production, income, and various social factors. He combines this with stratification methods to elaborate different layers within classes.

6.4.1. The elite

China's billionaires are testimony to the rapid rise of the capitalist class. In 2013 there were 212 dollar billionaires, 7500 yuan billionaires, and just over one million people are defined as millionaires (people with wealth exceeding 10 million yuan (approx. US \$1.6 million). The average millionaire is 39 years of age: half of them own a business; 20% are

investors; 15% are in real estate; and 15% are executives (Goodman, 2014, pp. 75–76). Half of China's entrepreneurs previously worked for the state or the party. Connections to the party remain a precondition for operating anything other than a very small business (Goodman, 2014, p. 83). Such connections facilitate access to resources, loans and permits, etc. Private sector elites originate overwhelmingly from inside the party-state. One report claims that 90% of China's millionaires are children of high officials (Dickson cited in Goodman, 2014, p. 88). In 2007, a survey found that 37.8% of private entrepreneurs were party members. Their influence in the state is illustrated by the fact that thirty-one billionaires were elected to the National People's Congress in 2013. However, half of China's wealthy people plan to emigrate (Goodman, 2014, p. 76).

According to Goodman, China's economic elite constitute about 3–4% of the population, when defined as those with an annual income in excess of 500,000 yuan (\$80,603 US) (Goodman, 2014, pp. 89–91). He combines the economic elite with the 500,000 leading cadres of the party and state to construct his definition of the 'dominant class'. But, in doing so, Goodman assumes a relatively stable correspondence of interests between the 500,000 leading cadres and the wealthy elite. However, the evidence shows that cadres and capitalists have contradictory material interests, and the conflict between these groups is rooted in the class structure of the state and society. The subordination of the capitalist class to the party and the state may help to explain why half of China's wealthy elite intends to emigrate⁴ including many better placed party leaders, and they also tend to send their children abroad, together with the significant resources. I believe that this indicates a lack of confidence in the security of their property and their position in society, and it illustrates the insecurity of those cadres who have accumulated wealth by illicit means.

6.4.2. The middle classes

In recent years the primary official objective in social class formation has been the creation of a large middle class. The middle class category is

said to include 'most state and social administrators, small and middle-sized business owners, managers, professional and technical personnel' (Zhao in Lu, 2012, p. 239). They are normally graduates who own a home and car (Goodman, 2014, pp. 95–96).

The middle class is seen as a buffer between the elite and the poor, as inequality provokes social antagonism and conflict (Hu, Li & Li in Lu, 2012, pp. 397–436). Lu claims that the size of the middle class is growing at 1% a year (Lu, 2012, p. 59) and will reach 35% of the population by 2020 (Lu, 2012, p. 55). The objective of the state's policy on class formation is said to be the creation of an 'olive shaped hierarchical structure' which is supposed to represent a modern class structure (Yang, Fang & Wang in Lu, 2012, p. 125). However, in official discourse the parameters of this middle class are diffuse and it appears to be more of a political objective than a social reality (Goodman, 2014, p. 93).

Academic estimates of its size vary from 5% to 28% and assume a minimum household income of about 60,000 yuan a year (about \$9670 US) (Goodman, 2014, pp. 102–103). However, large geographical cost of living disparities reduce the value of this benchmark figure, and higher income groups are more numerous in wealthier cities. Although homeownership is a common international determinant of the middle class, in China the rate of homeownership is very high at 89.7% overall, and it is 85.4% in urban China⁵ (Li Gan cited in Goodman, 2014, p. 115). So homeownership cannot be an effective determinant of class in China. A large expansion in higher education has also fostered the image of an expanding middle class as annual graduate numbers rose from 1 million a year in 2001 to 6 million a year in 2011 (Goodman, 2014, p. 112). Goodman concludes that the middle class comprises about 12% of the population, and is composed of entrepreneurs, office workers, professionals, and managers (Goodman, 2014, p. 119). They are divided between system 'insiders' and system 'outsiders' with 80% being insiders employed by the state (Wang and Davis Goodman, 2014, p. 120). Li Chunlin, using a broader definition of the middle class than Goodman, says that, although a drift towards the creation of a middle class inside

the private sector is evident, 62% of the better off middle class and 54% of the more marginal layers of the middle class work for the state.

‘This has resulted in an important feature of China’s middle class: public sector members have a closer relationship with the state than private sector members because they depend on the state for their socioeconomic well-being. Some of them, especially the upper new middle class, exert strong influences on policymaking and public opinion’ (Li Chunling in Li, 2010, p. 147). The fact that a big majority of the middle classes are state sector workers reinforces the intimate connection between public property and party interests. This illustrates the challenges that confront the reproduction of capitalist power relations through the existing state.

6.5. Are the capitalists a ruling class?

Mel Rothenburg takes up the question of whether China's capitalists can be said to constitute a ruling class. She explains that the transformation of China's class structure, alongside its rapid economic development, produced a society in which the working class and peasantry constitute the overwhelming majority of society. But bureaucratic interests that secure privileges for its members shape the inner dynamics of the party. However, ‘despite its monolithic structure, groupings and tendencies reflecting the politics of various existing classes and class factions’ and the internal politics of the CCP, ‘represent some fundamental visions and divisions about the path China should follow.’ (Rothenberg, 2015, p. 29)

Rothenberg uses a Marxist definition to define governing as the exercise of power through appointed positions of authority and believes that the class interests served by political power define the concept of the ruling class. Governance is directly based on the command of force, class rule may also exercise power by force, but it depends on consent or acquiescence, and relies on discreet forces and habits that ensure the social reproduction of existing class relations. A stable and developed system of power requires that governance and rule are separate - as

conflicts within the ruling class that endanger social stability need to be resolved by negotiation or force. If force is needed to resolve matters such force should be applied by a nominally independent state. Or if governments lose their authority, the ruling class can support another government but still remain the ruling class.

Rothenberg cites this illuminating analysis by Poulantzas: 'The state is not an instrumental entity existing for itself, it is not a thing, but the condensation of a balance of forces. The correspondence in question is established rather in terms of organisation and representation: the hegemonic class or faction, beyond its immediate economic interests which are of the moment or at least short term, must undertake to define the overall political interests of the classes and fractions that constitute the power block, and thus its own long-term political interest.'

(Poulantzas cited in Rothenberg, 2015, p. 30)

Rothenberg suggests that the capitalist class is the only viable candidate to be defined as the ruling class. But she says that the CCP acts as both the governing apparatus and a substitute ruling class. This endangers the system, as stable systems are based on a separation between the ruling class and government. Thus in Western democracies the ruling political party can lose office but this does not have to have any impact on the wealth and power of the ruling class. Rothenberg's chronology of Chinese reforms and the rise of Chinese capitalism claims privatisation was the primary source of capitalist primitive accumulation. She believes that before the 1980s the CCP was 'based on the peasants and workers' a legacy that 'continues to cast a deep shadow over the Party' (Rothenberg, 2015, p. 35). Capitalism does not dissolve the division of labour between the ruling class and the state, mainly because of the danger to social stability that this represents. However, the separation between the CCP and the capitalists does not itself, disprove the concept that capitalists are the ruling class. However, nor does the growing wealth and influence of the capitalists automatically transform them into a ruling class (Rothenberg, 2015, p. 36).

Rothenberg tries to locate the position of Chinese capitalists within ideological debates. There is an influential right-wing trend that wants China to evolve into a mature capitalist state, similar to advanced capitalist states, where the government and economy are run by, and for, private capitalists. The neoliberal proponents of this view tend to support the CCP, and seek gradual change. Many are western educated and are intellectually supported by the Western media and by mainstream economists, who garner support from the capitalists, sections of the middle classes, and those young people who are opposed to CCP rule. The ruling faction promotes a centrist position, based on the continued dominance of public ownership. Although, they support capitalist economic activity -the official objective is to modernize the economy and move towards a mature socialist society. Debates on the reform of SOEs, privatisation and fundamental reform have raged for three decades but they have never actually resulted in privatisation of the commanding heights. This faction is cautious and relies on taking measures that sustain and reproduce social stability whilst modernising. So they promote policies like extending welfare provision and labour rights that are an anathema to the neoliberals (Rothenberg, 2015, pp. 37–39).

Another tendency inside the party is based on leftist ideology and leans on workers, peasants and the poor for support. This found expression in the ideas and policies pursued by Bo Xilai which were supported by 'new left' intellectual currents outside the party. This tendency is clearly rooted in basic historical traditions of the CCP's socialist ideology (Rothenberg, 2015, p. 39).

6.6. Social strata within the working class

In classical Marxism the working class refers to those who live by selling their labour power for a wage and the proletariat are those employed by capitalists to produce surplus value (Draper, 1981, pp. 34–38) After the 1949 revolution in China a section of the workers were combined with officials of the party and state into a privileged category defined as 'employee-workers'. This category of workers referred exclusively to

those employed by state enterprises. They were also provided with extensive welfare rights and provisions known as the 'iron rice bowl'. Below this, were workers of lower status employed in collective enterprises, and under them, were various gradations with worse terms, conditions and rights. At the lowest rung were peasants, peasant-workers, seasonal, and temporary workers. The residence restrictions called the *hukou* entrenched this hierarchal stratification system.

Today China's working class is composed of different strata each with different status, wages, conditions and rights. The largest section of the working class occupies a position at the lower end of the spectrum. They are not legally recognised as being workers and so are not protected by labour laws, as they operate in the informal economy.

In the early reform era, peasants worked in rural industrial enterprises as a supplement to agricultural work. Later mass rural to urban migration was permitted. This generated an army of workers without status or rights: workers laid-off by state enterprises; workers employed in small-scale private enterprises; and people who engaged in individual economic activities. Huang, using Chinese census statistics from 2010 shows that the urban formal economy employed 36.8%, and urban informal sectors employed 63.2% of the workforce (Huang, 2013, p. 354). However, this ratio changed dramatically in 2013, when employment in formal sectors rose to 47% and informal sectors fell to 53% according to figures from the National Bureau of Statistics, which rely on the same data sources.⁶

The informal sector is composed of private enterprises, individual entities and unregistered workers. The category of private enterprises in China refers to incorporated entities. Private urban enterprises employed about 60 million people in 2010 with an average of 13 employees and registered capital of about \$200,000 US. In both rural and urban areas there were 6.24 million such private enterprises, employing a total of 90 million employees, an average of 15 per enterprise. Employment in this private sector rose to 125 million employees in 2013, composed of 82

million urban and 42 million rural employees.⁷ In 2010 individual entities (the urban self-employed) engaged 44 million people with an average of 2 people per entity - generally family members - but their average capital was a miniscule \$6,290 US (Huang, 2013, pp. 355–356).

Unregistered workers in the informal economy appear in government statistics as the difference between total urban or rural workforce and those employed in formally designated employment categories (Huang, 2013, p. 354). In urban areas this figure fell dramatically, from 113 million in 2010, to 90 million in 2012 and 60 million in 2013. This fall appears to be attributable to the government's drive to formalize migrant workers under its urbanisation plan.

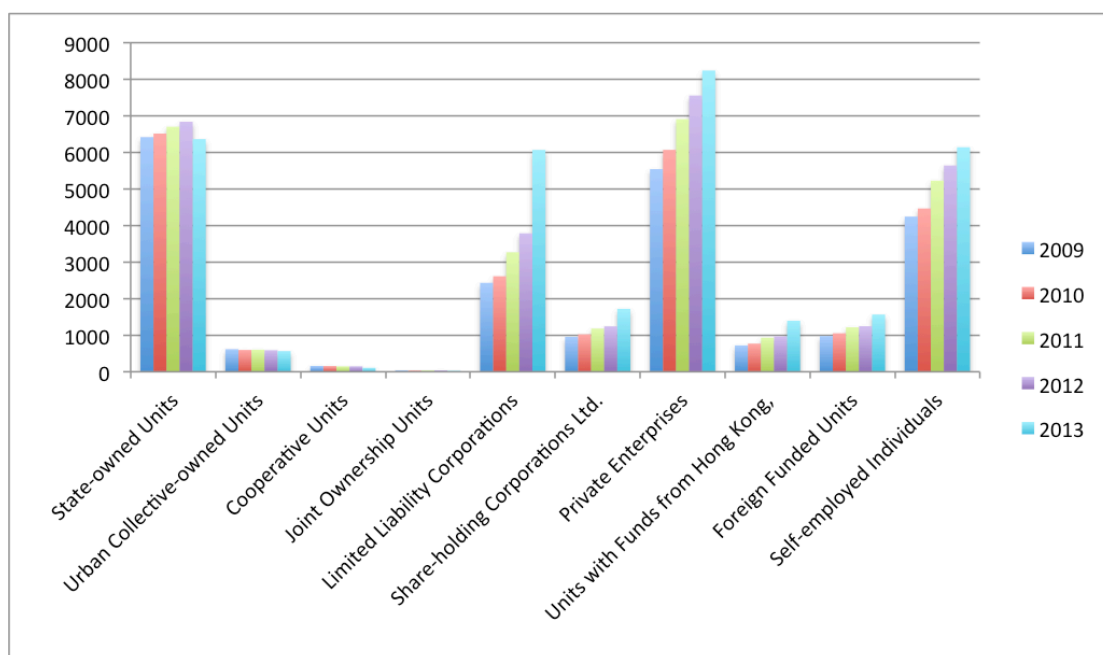


Figure 11. Graph of urban employment by ownership type 2009-2013

The graph above shows urban employment by sector from 2009-2013. The data is drawn from China's National Bureau of Statistics.⁸ Note the large rise in urban employment in Limited Liability Corporations of over 22 million in the year from 2012 to 2013. Share-holding Corporations grew by 4.7 million whilst employment in SOEs fell by 4.7 million; probably indicating a change of categorization of some SOEs into Share-holding entities.

Hired labour in agriculture does not exist as a statistical category in China and there seems to be no research on its exact scale. Rural statistics reveal that agriculture remains dominated by family farming with only about 3 to 10% of work being conducted by wage labour. This is in stark contrast with India where the figure for wage labour exceeds 45%. Nevertheless China's agricultural output value has risen by 6% a year for 30 years. Huang says it is the restructuring of food consumption and the corresponding shifts in agricultural production that drove this progress. In certain sectors, such as dairy farming, eggs, fruits and aquaculture, wage labour has grown to make up about 20-30% of labour-time based on capitalist farming. Nevertheless farms that account for 93% of China's sown agricultural land employ wage-labour for less than 10% of their work (Huang et al., 2012, p. 143).

6.6.1. Class stratification and CCP support

The bureaucracy is the gatekeeper to the cities for those with a rural residence status; as access to urban social provision, welfare, education, and housing is regulated and controlled. The stratification of classes in China has mainly been defined by *hukou* residency rules since the 1950s. Apart from during periods of political upheaval, the party has ensured that urban workers and cadres lived in secure and stable circumstances. State enterprises guaranteed the so-called iron rice bowl: the provision of cradle-to-grave welfare internal to workplaces. The quality of the contents of the rice-bowl was partly dependent on the importance and type of enterprise, with large state owned enterprises offering the greatest provision.

The difference between agricultural and industrial prices, known as the price scissors,⁹ was exploited to help finance urban development and peasants were able to move to the cities only under exceptional circumstances. This created a permanent entrenched division between urban and rural inhabitants. The price scissors in relation to China is

considered as the transfer from agriculture to finance industrialisation. In the 1950s it took the form of the compulsory deliveries of foodstuffs by procurement, where low agricultural prices were set by the state (Knight, 1995, p. 130).

After 1978, in the reform era, this rigidly stratified social structure remained the basic social foundation of China's planned economy and state. Transfers from agriculture to finance industrialisation continued in a different form (Knight, 1995, pp. 133–134). When the residence rules were relaxed and mass migration from the countryside in search of urban employment took place, the migrating peasant-workers provided low cost labour for all types of employment from locally owned Township Village Enterprises, to vast state financed construction projects, as well as to indigenous and foreign owned private sector enterprises. This system of stratification protected the existing urban workforce from downward pressure on their wages and conditions that would automatically occur in a free labour market when tens of millions of people with no labour rights compete for work. Indeed, the living standards of peasants and workers rose simultaneously.

6.7. The structural formation of the working class in China 1949-1981

This section examines the historical origin and structural formation of the China's working class from 1949-1981. It has been convincingly argued that an entirely new working class was created by the Chinese revolution (Walder, 1984) (Walder, 1986). The rate of accumulation and industrialization and the organization of the workers' lives was shaped and designed by the CCP within an external demographic environment that: *'limited improvements in the standard of living and dictated changes in patterns of growth, employment, and welfare.'* (Walder, 1984, p. 4) Proletarianization took place under bureaucratic control and the near universalization of public or collective property forms. The new working classes were rigidly stratified in a way that entrenched vast differentials in living standards, social security, welfare, and life prospects.

In the first eight years after 1949 private enterprises were nationalized. From 1949 to 1957 state owned industry more than doubled its workforce from 3 million to 7.9 million and even tiny enterprises were combined into large cooperatives (Walder, 1984, p. 6). Industrial output grew rapidly and a new regime of workplace power relations took the form of a bureaucratic hierarchy emulating that in the Soviet Union. The new workforce were employed, paid, trained and integrated into new state institutions based on '*worker dependence and managerial paternalism.*' Party and union entities controlled the formation of the working class and everyday workplace relations (Walder, 1984, p. 12).

China's planned economy was established in the 1950s. One unique aspect of the system was the *hukou* - a hereditary household registration system introduced in 1959. It bound people to their registration status at birth and was a powerful bureaucratic planning constraint. The *hukou* acted to limit rural-urban migration by rationing life essentials, which were tied to one's *hukou* location. There was a big rise and fall in the urban population at the time of the Great Leap Forward in the late 1950s but overall, from 1959 to 1978, only 329,000 people were permitted to move to the cities (Wang Chunguang in Lu, 2012, p. 269). This entrenched urban and rural divisions, which took three key forms:

1. Registration defined agriculture or non-agriculture as one's economic activity
2. Urban and rural administration and services were founded and operated on different principles.
3. Property rights in the countryside were collective, but in the cities there was public ownership and cooperatives.

The urban focus of government policies ensured that agriculture transferred vast resources towards industrialization and urban social services; both as direct transfers, and by means of the price scissors, which rigged the terms of trade against agriculture. Urbanization lagged behind industrialization. Indeed, from 1959 to 1978 the rural population (defined by *hukou*) actually rose from 17.92% to 18.41% of China's total population (Wang Chunguang in Lu, 2012, p. 271).

In 1949 China was composed of large cities and vast, dense, rural populations engaged in productive, but labour intensive agriculture. This limited the scope for urbanization. Between 1949 and 1957 the urban population rose from 57.6 million to 99 million. This was due to natural increases and rural-urban migration. The Great Leap Forward (1958-1960) involved vast labour mobilization - industrial employment rose by 15.8 million between 1957-8. The urban population reached 130.7 million in 1960, but fell to 100.7 million in 1965, after the failure of the Great Leap. Non-agricultural employment declined from over 50 million in 1960 to 32 million in 1963, only returning to its 1960 peak in 1971 (Walder, 1984, pp. 13–19).

Measures to prevent rural-urban migration were seen as the only means to avoid chaotic and uncontrolled population flows that might disrupt planned urban development. The collectivization of agriculture in 1957 facilitated the control of rural to urban migration because rural production teams distributed essential rations. The priority in urban areas was to employ urban residents; this was achieved by a low wages-high employment policy. The urban working class, and the urban population in general, were insulated from external demographic changes. However, in the period 1965-75, 16 million urban youths were 'sent down' to the country to 'learn from the peasants'. Millions returned to the cities between 1976-1979.

The annual number of youths entering the urban labour force for the first time was about: 1 million during the 1950s; 2 million from 1966-1976; and 3 million in the early 1980s. These numbers swelled to 5 million a year in 1977 because of the influx of sent-down returnees. Urban employment growth failed to satisfy demand. In 1980: 37% of new urban workers were sent to state enterprises; 43% to collective enterprises; 6% became self-employed; and 14% were allocated temporary work. Walder argues that rural proletarianization was completed in the form of collectivization in the 1950s, but proletarianization through urbanization was stopped and, indeed, reversed by 1980 (Walder, 1984, pp. 19–22).

Urban wages rose rapidly in 1949-1957, but then wages for state employees fell, from an average of 741 yuan in 1964, to 632 yuan in 1977 – 58 yuan below the 1957 level. As the workforce rose, entry-level wages were kept low and wages were generally frozen. Per capita housing space also fell from 4.3 square meters in 1952 to 3.6 square meters in 1977. Average per capita calorie intake declined slightly between 1957 and 1977 and was lower than Pakistan or Indonesia. The rationing of supplies compounded the burden of securing adequate daily nutrition. Differences between sectors of the urban working class were most evident in non-wage payments. Larger state enterprises provided all encompassing welfare provision: lifetime employment; sick leave; medical care for employees and their families; retirement provision etc. These enterprises might have their own hospitals, clinics, schools, crèches, canteens, cinemas etc. The average value of such non-wage benefits for state sector workers was equal to 527 yuan, or 82% of their cash wages in 1977. The long-term fall in wages was also countered by a rise in the number of wage earners per household. A decline in the average number of dependents meant that per capita urban income rose (Walder, 1984, pp. 22–25).

The limited capacity of state enterprises to provide employment meant that urban collective enterprises, which originally developed out of handicraft coops, grew. Similarly rural collective industries soaked up rural surplus labour. In addition, urban industries employed temporary labour forces. By 1980, 20 million rural workers were employed by what were the forerunners of Township and Village Enterprises (TVEs). They grew out of communes and brigades operating small scale collectively owned enterprises. These enterprises could not offer the benefits of urban enterprises and often employed workers seasonally. In 1982, 9 million rural workers were employed by urban enterprises temporarily, largely by informal means. Local labour bureaus would act as the labour suppliers and work was often seasonal. State enterprises contracted nearby communes to provide labour for a period of time or for specific projects. Similarly, urban residents could find temporary work with state enterprises on terms somewhat better than their rural counterparts, but

these workers didn't have farms to return to, to act as a safety net (Walder, 1984, pp. 28–33).

In 1980 there were 15 million employees in urban collective industrial enterprises administered by local governments. These workers received lower wages (an average of 632 yuan in 1981) and less social security than state enterprise employees. The larger the enterprise, the more stable and secure the employment, and the more the firms were integrated into planning. These firms employed a predominantly young and female workforce. By 1980, such collective enterprises were assigned 43% of urban job allocations. Such employment excluded later transfer to state enterprises (Walder, 1984, pp. 34–36).

State enterprises employed 34 million workers in 1981. They were the best provided for in terms of the welfare rights known as the *Iron Rice Bowl*. They made-up 42% of the urban workforce, produced 75% of industrial output, and average earnings were 854 yuan a year. They were guaranteed lifetime employment, gradually rose up an 8-grade wage scale, and received comprehensive welfare provision. The larger the enterprise the greater the benefits (Walder, 1984, pp. 37–38).

Growth of the labour force was greater than the capacity of the capital-intensive state sector to employ new workers. Average investment in fixed capital per worker was 10,000 yuan in the state sector, compared with 2000 yuan in urban collectives, and 950 in rural collectives. So a relative decline in the percentage of workers employed in the state sector was inevitable. Workers in state enterprises were often able to secure employment for their children within the enterprise, creating a closed entry system. Demographic conditions contrasted sharply with the USSR where labour shortages and job mobility became commonplace in the 1980s. Consequent divisions between sectors of the workforce were far less pronounced in the USSR than in China. The engrained inequalities in China, particularly between urban and rural, were extraordinarily rigid.

In 1980 China's urban workforce was highly stable and fixed, in the state and urban collective sectors. Workers' families pooled incomes to increase their consumption. The increase of the urban working class by means of urbanizations was halted. However, proletarianization took place through rural industrialization via commune enterprises, which then became TVEs. Markets did not define workers' lives. Instead, their prospects were determined by their residence status, and by the type of enterprise they worked in.

This system divided the working class. The state enterprise workers were... *'absorbed into the lower statuses of an economic bureaucracy' ... 'their consciousness was increasingly dictated to them by bureaucrats in a Party claiming to be their historical agent'* (Walder, 1984, p. 42).

6.8. The structural formation of the working class in the reform era

The urban-rural gap declined from 1978-1985, farmers were permitted to sell their surpluses and do non-agricultural work, and both township village enterprises (TVEs) and private firms grew.¹⁰ From 1985-9 these rural enterprises boomed, private sector industry also advanced rapidly in some urban areas, particularly on the eastern seaboard. Labour migration to the cities became a flood. In 1989 the independence of township village enterprises was repressed.

Between 1992-2001 urban State Owned Enterprises were restructured resulting in millions of layoffs, the corporatization of many of the largest enterprises, flourishing foreign investment, and tax policies favouring central government. Urban state entities gained from land sales and their domains of influence expanded with urban growth. The urban-rural gap continued to rise. With TVEs performing badly, rural conditions worsened. Social unrest amongst the peasantry increased and migration to the cities generated a rural crisis. In response, the state abolished agricultural tax and invested in rural social security between 2003-5. However, despite relaxing registration restrictions on migration to urban areas, the floating population continues to experience a form of social

apartheid in the cities. This is expressed in their restricted rights to: housing; education; healthcare; pensions; employment rights etc. (Lu, 2012, pp. 274–278).

Human development inequalities in China are largely defined by the urban-rural gap. China's urban inhabitants are ranked at position 30 on the UN's world human development index. That is close to South Korea. However, the position of China's rural inhabitants is 125th in the world index. That is close to Botswana. Power, wealth and resources are concentrated in the cities. The working class is the largest social class in urban areas. The transfer of resources from rural to urban has accelerated since 1978. It takes the form of a flow of finance; land acquisition; and the exploitation of rural migrants (Lu, 2012, pp. 283–287).

The dominant forms of objective class analysis in present-day China divide people into the following occupations or strata:

'State and social administrators, managerial personnel, private entrepreneurs, professional and technical personnel, clerical personnel, individual-operated business proprietors, commercial and service personnel, industrial workers, agricultural labourers, and the unemployed and partially employed.' (Guo, 2012, p. 734)

Inequalities are presented as part of the technical division of labour rather than as products of exploitative relations. Guo (2012) points to a trend to fetishize an idealised middle class; when, for example, they are presented as incarnations of progressive thought and a harmonious future. The official promotion of an olive-shaped form of societal wealth distribution, acts to reinforce a middle class ideal. Mao had earlier called China egg-shaped. This not only de-emphasises the working class; it also allows the identity of the bourgeoisie to be cloaked under a middle class mantle. Guo sees this as an expression of the failure of official ideology to find a consistent and adequate theoretical justification for the real class relations that have developed over recent decades (Guo, 2012, pp. 737–738).

The National Bureau of Statistics (NBS) estimated a total rural workforce in 2007 of 476.4 million, 150.9 million employed in Township Village Enterprises, 26.7 million in private enterprises, 21.9 million self-employed, and 276.9 million 'others' a category composed of all 'agricultural, migrated and surplus labourers.' The migrated, defined by living more than 6 months in urban areas, constitute approximately 150 million workers (Cai and Wang, 2010, p. 74). Many take seasonal work in urban areas and are also part-time farmers. The fluidity of rural-urban migration makes identifying the number of pure farmers difficult, and there are no statistics on this. But if we deduct 150 million migrants from 'others' we're left with about 126 million (Yang, 2013).

The concentration and centralization of employment location is a feature of the growth of private sector investment since 1978. China's centres of world manufacture are creations of the reform era. They are concentrated in eight areas: Shanghai, Tianjin, Zhejiang, Jiangsu, Guangdong, Fujian, Shandong and Hebei. The main concentration of industrial investment and employment pre-1978 was in the North East of China. And the urbanization of the west of China lags nine years behind that of the east.

Private sector urban employment mushroomed from 0.68 million in 1992 to 45.8 million in 2007. Urban self-employment grew from 150,000 in 1978 to 33.1 million in 2007. Employment in joint stock enterprises (corporations, limited liability companies and joint-stock companies) grew from 1.64 million in 1993 to 30.3 million in 2007.¹¹ Employment in foreign and Hong Kong and Macao companies grew from 600,000 in 1990 to 15.8 million in 2007. State enterprises reached a peak employment of 112.6 million in 1995, but this fell to 64.2 million in 2007 (Lu, 2012, pp. 143–144).

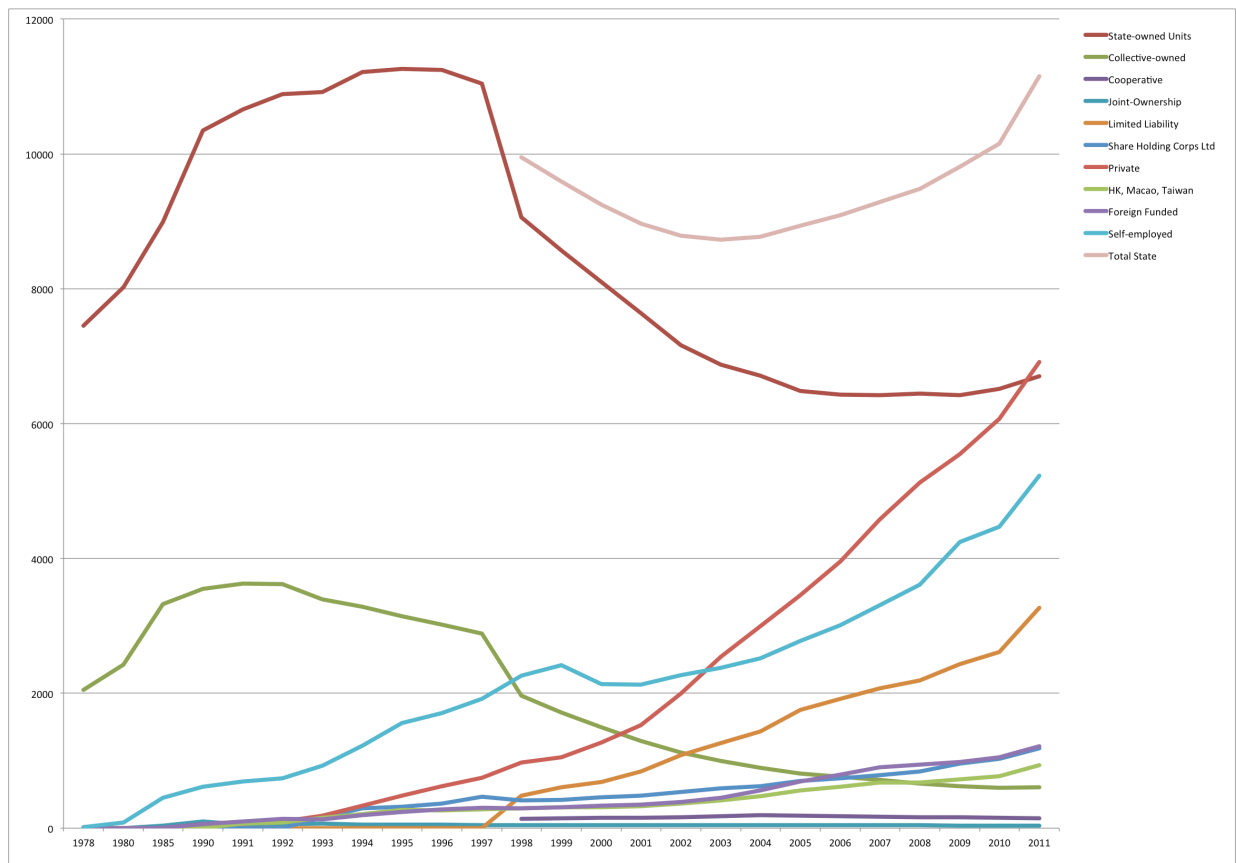


Figure 12. Chart of changes in urban employment by ownership type 1978-2011

Figure 12 above charts changes in the number of urban employees (unit: 10,000 people) by ownership type from 1978-2011.¹² It includes a category labelled “total state” which combines the workforce of State Owned Enterprises, Limited Liability Corporations and Share Holding Enterprises. This definition of the total state owned sector broadly corresponds to the arguments made by Huang (2008).

Production workers are a large percentage of the workforce in Zhejiang 43.7%, Tianjin 39.1%, Shanghai 36.2%, Guangdong 35.3%, Jiangsu 31.5%, and Fujian 31.2%. Business people of all types are highly represented in the same provinces: Zhejiang 11.6%, Guangdong 10.9%, Jiangsu 9.4%, Fujian 10.2% and in Beijing they constitute 15.8% of the workforce (Lu, 2012, p. 159).

Workers with rural registration constitute 52.4% of non-agricultural employees. They make up the largest section of the working class. They

compose 67% of those employed in secondary industry and 40% of those in tertiary industry. In the following seven industries they are the majority of the workforce: construction 97%; manufacturing 68%; resident and other services 61%; accommodation and catering 59%; wholesale and retail 53%; mining 51%; transport, postage and storage 51%. Migrants also make up: 34% of technical and professional staff; 33% of administrators of government and party organizations; and 28% of clerical and related staff (Lu, 2012, pp. 155–156).

Various occupations within the total workforce changed as follows in the years 1982 and 2005: managers of enterprises and institutions, 1.1% to 1.2%; clerical staff, 1.3% to 3.1%; business personnel, 1.8% to 7.0%; service workers, 2.2% to 5.2%; production and transport workers 16% to 17.9%. Rural workers in agriculture, forestry, fishery, animal husbandry and water conservancy fell from 72% to 57% of the total national workforce during the same period (Lu, 2012, pp. 150–151).

Labour relations shifted in favour of employers in important ways. Absolute employment stability was replaced by flexibility in hiring and firing, particularly in new and private workplaces. The enhanced power of employers over workers, particularly migrant workers, resulted in increased labour intensity and duration. Employers often ignore health and safety and have scant regard for their legal responsibilities. This generates high death, injury and sickness rates.¹³ The workers share of GDP declined from 53.4% in 1996 to 39% in 2007. The 'earned surplus' of enterprises as a percentage of GDP increased from 18.8% in 2001 to 31.3% in 2007 (Shi Xiuyin in Lu, 2012, p. 170).

6.8.1. The impact of mass unemployment on wages

The vast lay-off of workers in state owned enterprises between 1998–2001 is commonly seen as marking a watershed in Chinese labour relations by destroying workers' rights. Thus Tim Pringle, a scholar of Chinese labour relations, says, 'figures are staggering: 25.5 million workers made redundant in 3 years! How did the Communist Party of

China succeed in tearing up the so-called social contract between the party and the working class?’ (Pringle, 2013, p. 194)

Yu claims that 60 million workers were sacked between 1995 and 2003 - ‘a scale never seen in history’. He says that state owned enterprises and collective enterprises provided ‘good jobs’ which were replaced by ‘bad jobs’ and ‘a great social regression’ (Yu, 2011, p. 144).

Laid off workers were generally categorised as *xiagang*: this meant they remained tied to their work unit but were not engaged in employment. This provided some cushion particularly in larger enterprises where extensive welfare provision existed, but many other *xiagang* workers relied on family support.

Such a dramatic rise in unemployment would cause a fall in wages in a free labour market. However, between 1992 and 2007 the average real wage of all workers rose by 202% and the wages of state sector employees rose by 260% despite layoffs (Ge and Yang, 2014, p. 1).

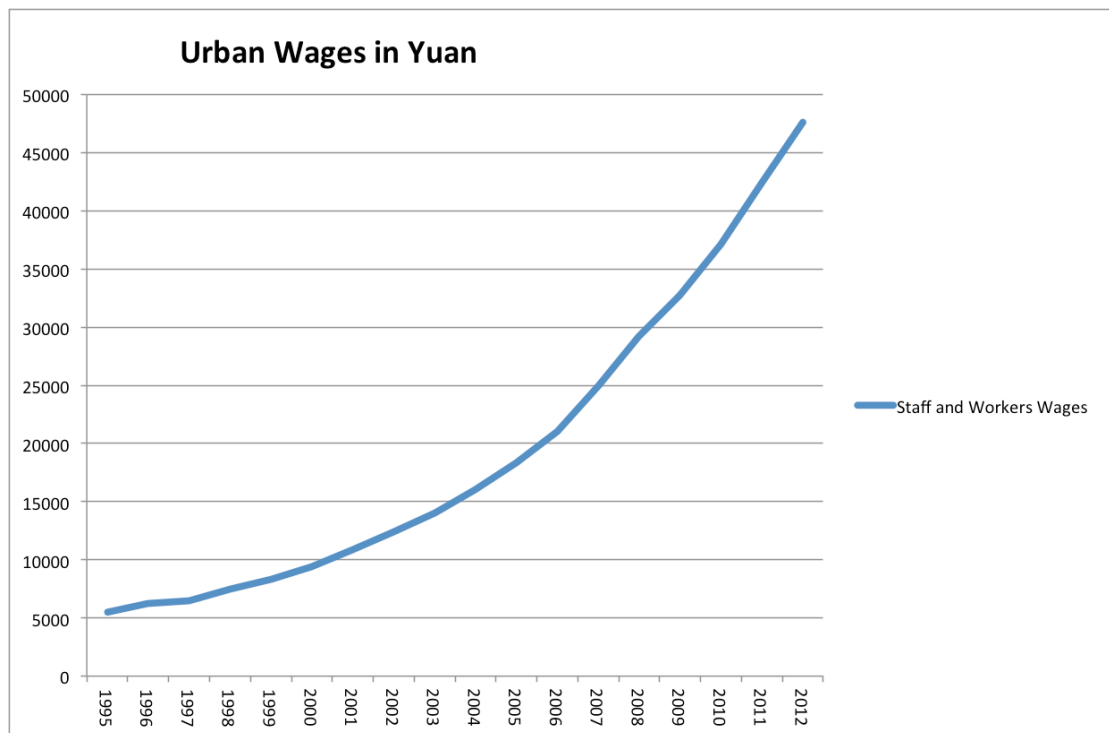


Figure 13. Chart on the wages of urban workers designated as staff and workers

Figure 13 shows the rising wages of urban staff and workers (formally employed workers) from 1995-2012. ¹⁴

Noteworthy too is the fact that wage rises were highest amongst state employees. State owned enterprise wages overtook private sector wages in 2003 and the gap has increased since then. Thus private sector enterprises are compelled to offer higher wages to attract talent (Yang et al., 2010, p. 487).

How could the vast shake out of 25-60 million urban workers simultaneously produce sharply rising wages? One explanation is that the reduction in costs to state enterprises generated a rise in productivity and retained state employees benefitted. Also, some geographic and demographic component could have been partially responsible, as older workers were more likely to be laid-off in regions dominated by state owned heavy industry, the so-called rust belt of Northeast China. These laid off workers were either, not in the market or weren't considered suitable for work in Southeast China's private, foreign owned, or joint venture companies.

More recently the cause of rising wages was sought in demographic factors. Pringle says labour shortages began to appear in early 2003 *'initially confined to skilled and experienced workers required in coastal provinces, the shortages have spread to other areas of the country.'* As a consequence *'the balance of forces has tipped from capital toward labour.'* (Pringle, 2013, p. 197) As China's working age population begins to shrink from 2015, the shortage of urban labour will put migrant workers in a position to demand a *'substantial enhancement of wages and other incentives'* to replace the declining urban labour force (Cai and Wang, 2012, p. 8). Cai and Wang believe China is at the *Lewis Turning Point*: a moment when expanding labour demand exceeds labour supply - causing wages of unskilled workers to rise (Cai and Wang, 2012, p. 9). However, national data shows that the wages of unskilled workers have

risen consistently since 1992, eleven years before the Lewis turning point is said to have arrived (Ge and Yang, 2014, p. 10). If so, it seems that market forces aren't the primary determinant of wage rates in China.

6.8.2. Trade Unions: structural and associational power in the reform era

Within the CCP led state system the main agency that is supposed to represent the workers is the All China Federation of Trade Unions (ACFTU). It is a bureaucratic organization and the sole official representative of the workers. Feng Chen's (2009) study of the power of the ACFTU uses Wright's distinction between associational power, stemming from collective workers' organisation, and structural workers' power, derived from the union's strategic position within the economic system. I look at the ACFTU's structural power and then at spontaneous associational forms of workers' power during the reform era.

The ACFTU was formed as a militant workers' organisation in 1925. However, after 1949, the union generally acted as a transmission belt to assist the party and management to increase production and promote party ideology. The ACFTU's was designated as the sole representative of workers' interests from 1949-66 but this status was subsumed under the CCP's general claim to have established a socialist state that eliminated fundamental class contradictions. The ACFTU's limited influence was revealed by its position in the party hierarchy. It acted as a workers' welfare agency and dealt with such issues as wages, labour protection and insurance, housing, sport, and cultural activities. During the Cultural Revolution (1966-1976) the ACFTU ceased operating entirely, yet paradoxically, it was in 1975 that the right to strike was included in the constitution.

When the ACFTU was revived under Deng Xiaoping in 1978, leading cadres of the union took positions in the Politburo. However, the right to strike was removed from the constitution in 1982 following the strikes in Poland led by Solidarity. The ACFTU was allotted the role of maintaining stability in times of radical social transformation. Four new departments

were created which enhanced the ACFTU's portfolio of institutional power.

Their ambit is 'collective contracts, democratic management, legal affairs, and grassroots organizational construction. By design, these new departments tend to be more proactive. They were created to work in new areas that have emerged with the market reforms, and thus are expected to initiate, explore, experiment with, and establish new rules and practices suitable for changed labour relations. These departments, in other words, are more action oriented.' (Feng Chen, 2009, p. 671)

At the time of the Tiananmen Square protests in 1989, the ACFTU expressed support for the students, but new independent workers' organisations, like the Beijing Autonomous Workers' Federation (BAWF), claimed the right to supplant the ACFTU as the voice of the workers. The Party leadership saw these organisations as a direct challenge to CCP rule. Thus, after the suppression of the Tiananmen Square protests, plans for greater autonomy for the ACFTU were shelved.¹⁵ The ACFTU's bureaucratic authority was enhanced to facilitate closer supervision of urban workers and of the union itself. It became increasingly interconnected with the government apparatus. This integrated the union more closely with the party and state and afforded it greater scope and power within which to operate (Feng Chen, 2009, pp. 667–671).

Feng notes that the ACFTU plays a significant role in promoting legislation that advances the rights of workers. Its power derives from being an official institution of the state subordinate to the party. It operates as a governmental agency and its structure parallels that of the party and state. Feng sees local union cells as being in an embedded relationship to company management (Feng Chen, 2009, pp. 663–664).

The ACFTU's role within the state bureaucracy became increasingly important as market reforms and the growth of capitalist labour relations provoked workers' unrest. The status and influence of ACFTU cadres at all levels of the state bureaucracy grew. They were expected to manage

labour relations. However their role in grass roots labour mobilisation has been negligible. Union officials are often managers or party appointees rather than being elected from below. Where labour protests break out the union generally intervenes as a mediator whose authority derives from its governmental status (Feng Chen, 2009, pp. 665–667).

The ACFTU's legal department proactively drafts legislation and supports its implementation by establishing legal service centres: in 2000 there were 2,363 with 4960 staff; in 2006 there were 3,856 with 11,059 staff¹⁶; and in 2007 there were 6,178 with 18,433 staff.¹⁷ This mechanism ensured that a high percentage of worker's legal cases were wholly or partially successful.¹⁸ One might say that the legal sphere is a terrain of class conflict mediated through bureaucratic forms. The following exasperated blog from an attorney acting for foreign companies in China is indicative of the view of business interests.

'I know a German factory in a first tier city here [in China] that hired the wrong Finance Director. When they let her go, she took them to arbitration. The factory had followed the law in how they hired her and in how they let her go. However, even after following the law, they still had to pay an extra three months salary beyond what they had already offered her. The decision shocked the German company...

'Every story I have ever heard of a foreign company going to arbitration in China against a terminated employee ends similarly (or much worse). The foreign company pretty much always loses. I think this is not so much because the foreign company is a foreign company but because China is still a communist country and workers' rights are still (at least in theory) paramount.'¹⁹

With the growth of the private sector and multinational investments, the ACFTU straddles the division of interests between capital, labour and the state. Scholars have emphasised the problems of trade union legitimacy that this role engenders (Xiaoyang and Chan, 2005)(Shen, 2007). Nevertheless, the ACFTU has promoted changes from above, which significantly improve the legal rights of the working class, like the 2008

Labour Law. These new legal rights often act as a focal point around which workers' activism is galvanized.

Occasionally there are signs that reformers within the ACFTU are trying to engage the key issue of fostering democratic workers' representation. At a structural level the union organized an extraordinary unionisation drive in recent years. Unionisation grew at incredible speed. Membership was 87 million in 2001, 239 million in 2010,²⁰ and 280 million in 2013.²¹ Studies indicate that the decision to join the union is overwhelmingly a voluntary act, with persuasion by shop stewards more common in private companies.²² The growth of the ACTFU and the spread of collective bargaining and collective contracts are legal and organizational measures designed to regularize labour relations.

One example of the ACFTU taking grass roots organization seriously was the unionization campaign at Wal-Mart. At a clandestine meeting on 29 July 2006, 25 workers in Quanzhou City took on the largest corporation in the world and won. They formed the world's first Wal-Mart trade union committee. The mood was said to be euphoric and workers sang the Internationale as Ke Yunlong, a 29-year-old meat-packer, was elected to represent the workers. Subsequent grassroots action led to a campaign by the ACFTU to rapidly unionize all Wal-Mart stores in China, this campaign followed a call by President Hu Jintao to build party organizations and trade unions in foreign-invested enterprises (Chan, 2006).

Analysis of workplace unions indicates that although the trade unions are generally controlled from above and are intimately connected to party organisations, there is nevertheless a notable degree of flexibility. At the fringes a variety of official representative entities and institutions this flexibility takes on forms that are genuinely voluntary, associational and at times are militant.

Research into the outlook and practices of trade union chairpersons indicates that in a significant minority of workplaces, workers utilize

workers' congresses and official union structures as avenues to express grievances and competitive democratic elections for union presidents take place. These processes tend to be more frequent in state or collective enterprises rather than private or foreign funded enterprises (Hishida, 2010). The increasing differentiation and complexity in work environments has brought about variations in forms of workplace representation by the unions.

The ACFTU represents workers as a structural power whose position in the political and state bureaucracy enables the union to play the pivotal role in designing and enforcing labour laws that enhance workers' living standards and workplace rights, the union also imposes compromises on employers. As a general rule, the ACFTU does not act as an agency of associational power in Wright's sense. However, it champions labour laws, which often become the focal point around which the associational power of the working class is organized and mobilized. There are also rare but significant instances where the ACFTU instigates or supports workers' associational activity, either with support from the national CCP leadership or with the support of grass roots union cadres.

6.9. Workers' associational power in China in the reform era

6.9.1. Tiananmen and the events of 1989

'1949 China overthrows Capitalism

1979 Capitalism saves China

1989 China saves Communism

2009 China saves Capitalism'

A Chinese viral Internet joke

In popular consciousness the fall of the Berlin Wall in 1989 is symbolic of the end of communism. The upheavals of 1989 began as student

protests in Tiananmen Square, Beijing. These protests were repressed on 4 June 1989. But subsequently a wave of revolts shook other states ruled by Communist parties across the Eurasian landmass.

Students led the protests in China, which began on April 15th by mourning the death of former General Secretary of the CCP, Hu Yaobang.²³ Protestors raised slogans against corruption and profiteering, and for democracy. Au and Bai see the movement on Tiananmen Square in 1989 as the culmination of increasing unrest amongst the working class at the consequences of market reforms, anger at corruption, and a sense of being betrayed by party leaders. They cite as evidence Deng Xiaoping's actions in banning the right to strike in 1982; promoting entrepreneurial rights and private property; collaborating with world capitalism; and keeping Hong Kong capitalist after its return to China in 1997 (Au et al., 2012).

Many workers visited the Tiananmen protests, were supportive of the students' demands, and joined in their debates. A small group of workers formed an independent workers' organisation called the Beijing Autonomous Workers' Federation (BAAF), to defend the students and promote this new movement amongst the working class. BAAF demanded wage rises, price freezes, and income declarations from officials. BAAF was only open to workers. It initially declared adherence to the national constitution and sought to develop an alternative to the ACFTU.

The students sought dialogue with the party leadership but intransigent responses in the party press provoked a student hunger strike. This increased the sympathy and support of the working class. 'Under heavy pressure from their own members, the ACFTU donated 100,000 yuan to the students. Cadres from the official trade unions took part in demonstration (sic) to express solidarity with the students.' (Au et al., 2012, p. 138)

Lower level ACFTU cadres and students called for dialogue with the students; a free press, monitoring of officials, punishment of corruption, political reform, trade union reform, and self-management of the unions (Au et al., 2012, pp. 134–138). BAWF called for ‘an honest and incorruptible Chinese Communist Party, one which has the Chinese proletariat as its mainstay’ (Au et al., 2012, p. 139).

Autonomous workers’ organizations developed in various cities. In Beijing BWAFF’s influence increased and its demands became more radical. On May 19th they called for a one-day general strike if the government did not accept the demands of the students. Even though BWAFF’s declarations claimed to speak as the voice of the workers and the leadership of the movement, it never became powerful enough to make their strike calls materialize.

A split in the leadership of the CCP on how to handle the conflict led to the resignation of Zhao Ziyang, then General Secretary of the party. He went to Tiananmen Square, tearfully apologized, and pleaded with students to end their hunger strike. His plea was ignored and he was placed under house arrest until his death in 2005. On 20 May martial law was declared and troops entered Beijing. Protestors erected barricades to stop troop-carrying trucks from reaching central Beijing and attempted, with some success, to fraternize with soldiers. Troops withdrew on 24 May. Student leaders remained hostile to workers’ participation and often held rather elitist views about their superiority over the working class.

At the end of May Beijing government enterprises were instructed to dock the pay of those workers who join the protests, which Yu claims ‘*explains a temporary decline in the number of workers participating in the events.*’ (Au et al., 2012, p. 142)

Troops re-entered Beijing on 4 June, forcibly removed barricades and cleared Tiananmen Square - the focus of the protests. Yu argues that the movement was defeated because it underestimated government

determination, and the autonomous workers' movement appeared too late and lacked experience.

6.9.2. Associational power after 1989

When resistance to privatisation and the restructuring of state owned enterprises came to a head in the late 1990s. Overt workers' unrest by state employees from the 1990s until 2002 often drew on Maoist ideology and slogans. Friedman and Lee argue that these protests slowed down privatisation, 'convincing the state to hold on to a significant number of large enterprises' (Friedman and Lee, 2010, p. 518).

Radical changes in labour contracts and welfare provision increased the power of employers and shifted welfare provision outside of factory walls by means of contributory insurance plans. New labour laws were largely ignored by private and foreign enterprises, which provided most new employment opportunities in urban areas. Labour unrest in the mid-1990s often took the form of *'short-sit ins outside local labour offices aimed at provoking government officials into ordering capitalists to obey labour laws'* (Pringle, 2013, p. 196).

Legal measures to address grievances have become a focal point for workers' unrest. Claims and disputes taken to arbitration rose dramatically throughout the last 20 years, both for individual and collective cases.²⁴ This has been particularly evident in high growth regions. Workers and state bodies treat arbitration seriously. In the event of local officials conspiring with employers, workers commonly resort to collective action to secure the active intervention of higher-level government agencies (Friedman and Lee, 2010, pp. 517–518).

In chapter 3, we found that fundamental features of János Kornai's description of a reform socialist system²⁵ remain dominant in China. This framework can help us to assess some unique characteristics of current workers' struggles and the balance of power relations in China. One

pertinent observation made by Kornai was the tendency for self-management to emerge under conditions of reform socialism.

In China, as a concession to the workforce in the process of reforming state enterprises, increasing lip service was paid to the democratic management rights of the workers as defined in the constitution. Under articles 16 and 17, state-owned and collective enterprises 'practise democratic management through congresses of workers and staff and in other ways in accordance with the law.'²⁶ The process of restructuring in state-owned enterprises often gave rise to conflicts. The organisational focus for some successful forms of resistance was the 'Staff and Workers' Representative Councils' (SWRC), which are legally entitled to veto and control management (Xiaoyang and Chan, 2005)(Phillion, 2009).

Chapter 5, Article 52 of the Enterprise Law defines the rights of the SWRC thus:

- '1. To be informed and to examine major strategic policies such as long-term plans, annual plans, basic investments, reinvestment plans, plans for leasing and subcontracting, and so on;
2. To examine, agree to, or veto policies related to wages, bonus and industrial safety issues, and regulations pertaining to penalties and merits.
3. To examine and decide on policies related to the staff and workers' welfare, distribution of housing, and other important welfare matters.
4. To monitor and assess the performance of responsible cadres at each level and to make suggestions on how to reward, penalize, and dismiss them; and
5. To elect the factory manager according to the arrangement of the supervisory government bureaucracy, and to report the election results to the said bureaucracy for approval.' (cited in Xiaoyang and Chan, 2005, p. 12)

These legal rights can become a sharply contested domain of struggle within workplaces. And they are not simply remnants from a distant

Maoist past. For example, in 2010 the Shanghai Municipal People's Congress adopted comprehensive regulations seeking to extend the Workers' Congress system throughout all Shanghai enterprises regardless of ownership type.²⁷

Extremes of labour exploitation and abuse in contemporary China have come to global attention. They particularly shock those nostalgic for the slow pace of work and ubiquitous welfare provision in many urban state owned enterprises in the 1980s. In recent times cases came to light which shocked the nation: workers beaten and subject to ritual humiliation; children sold as slaves to work as beasts of burden in brick kilns, some of them were beaten unconscious and thrown into mixers.

Foxconn, one of the largest employers in the world, manufactures for major global brands like Apple, but only young people can cope with the intensity of work. The factory regime is strict and punishing, and the isolation of individual workers is rigorously imposed in their vast factories. The regularity and copycat nature of suicides, by jumping from a height inside the factory, made world news and safety nets were put up around the factory to prevent suicides. Fines, illegal detention, delayed wage payments, abuses of authority, and all manner of ruthless and barbaric exploitation often used to control labour discipline in private and foreign enterprises.

In 2004 only 12.5% of migrant workers with rural residential status were employed on a labour contract. In 2006 a State Council research team reported that the majority of migrant workers were paid irregularly or late, 68% had no rest day (Friedman and Lee, 2010, p. 510). However, a campaign to stamp out the prevalence of wage arrears amongst migrant workers was initiated by former Premier Wen Jiabao in 2004. After this, the percentage of migrant workers experiencing wage arrears fell dramatically (Meiyan, 2009, pp. 157–160).

Labour laws introduced in 2008 led to an increase in labour unrest. Disputes are defined as '*workers' initiation of labour disputes and other*

collective actions such as complaints and strikes.' (Cai and Wang, 2012, p. 11) Disputes increased every year. There were 169,000 disputes in 1999, but numbers doubled to 931,000 in 2008, and then fell slightly in 2009. Disputes are categorized as 'accepted' (the majority) or 'mediated'. 'Accepted': means labour arbitration bodies dealt with them. 'Mediated': means cases resolved before reaching arbitration.

In the year to 2008 disputes increased by 98% in the east, 50% in the centre, and 61% in the west of China. Disputes in the eastern region made up 76% of all disputes in the same year and are more common relative to urban employment there. The more developed provinces have the highest incidences. The poorest areas have far fewer disputes. In the first half of 2009, disputes affected 25% of state owned and collective enterprises, 7.5% of private enterprises, 13.8% of foreign invested firms and 11.8% of others (this category includes joint ventures, limited liability and joint stock companies) The larger the enterprises the higher the incidence of disputes: 36.8% of companies employing more than 1000 workers reported disputes in 2008 (Cai and Wang, 2012, pp. 12–16).

The main reason for disputes were wages (43% locals, 48.6% migrants), wage arrears (8.5% locals, 34.4% migrants) labour contracts (21.7% locals, 0.6% migrants), working time (17.1% locals, 0% migrants), workplace safety (7% locals, 14.8% migrants) and welfare disputes (2.6% locals, 1.7% migrants) (Cai and Wang, 2012, p. 19).

Informal and flexible labour employment was often organized in the form of dispatched labour (labour organized to work at a location for a specific time by a labour supplier). The 2008 Contract Labour Law permits the use of dispatch labor to fill '*temporary, auxiliary or substitute job positions*'. However, the practice spread from foreign enterprises to private and state owned entities as a means of bypassing the legal responsibilities and obligations that would apply to workers on full-time contracts. In 2010 a survey of the All China Federation of Trade Unions (ACFTU) reported there were 60 million dispatch workers.²⁸ However the

legal loophole was closed in December 2012 by amendments to the Labour Law.

Freidman and Lee describe the political economy of Chinese employment as being based on the authoritarian and monopolistic power of the CCP over society. This has three characteristics that shape relations with the working class: local accumulation aids and abets pro-capitalist actions by local government; rule by law seeks to legitimize official channels by mediating and controlling the regulation of labour related issues; and the migrant labour system ensures that unrest tends to be limited and localized (Friedman and Lee, 2010, pp. 514–516).

Protests by migrant workers tend to respect legal channels until/unless they appear exhausted or inadequate. Then, the protests may involve strikes, blockades, sit-ins or the threat of mass suicide. Some cases involved killing bosses or kidnapping them. Factory occupations and riots also appear as part of the armoury of tactics used by migrant workers.

Freidman and Lee look to autonomous workers' organisations as the remedy to the ACFTU's failure to represent at a grass roots level. They argue that there is an embedded relationship between employers and union officials, and there is an engrained and fundamental opposition to independent trade unionism in the ACFTU and the CCP. Independent labour NGOs and advocates engage in advisory work, which is generally aimed at rights awareness, but this can also lead to direct participation in disputes.

However, the 2008 Contract Labour Law significantly improved the legal position of the workers. Contract workers now have far greater security of employment; jobs for life automatically follow after two-contract terms or 10 years employment. The provision of severance pay has also improved. Freidman and Lee view the promotion of formal employment as a mechanism for the state to control labour unrest by channelling it into safe legalistic pathways. They acknowledge that the burden this

places on labour bureaus exceeds their capacity to process them and foresee an inevitable rise in labour unrest.

In April 2007 a strike by dockworkers in Shenzhen spread to another port in the city, and pushed the Shenzhen Federation of Trade Unions to intervene on the side of the workers. The general tendency is for such outbreaks of unrest to come to a partial or full victory for the workers' demands (Friedman and Lee, 2010, pp. 518–520).

In 2008-9, when the world economic crisis affected Chinese exporters most sharply, many employers absconded without paying wages. Angry protests by workers followed. Workers anger led local governments to put pressure on employers to limit the negative impact of the economic crisis. Cases of overt collusion in maintaining illegal employment practices, or of local government turning a blind eye to Contract Labour Law provisions were also evident.

Yu Jianrong works at the Social Problems Research Centre of the Rural Development Research Institute of the Chinese Academy of Social Sciences and is probably the most influential scholar monitoring social unrest in China. He identifies several characteristics of mounting worker discontent. These include, the sudden and spontaneous nature of disputes, the disbelief in official responses, the distrust of local authorities, and the faith in national government.²⁹ Protests generally concentrate on rights specified in the law. The availability of modern means of duplication and access to information has enabled militancy to be energetically channelled into exposing the discrepancy between the arbitrary nature of the exercise of power on a local level, and the contrasting positive legal rights of the poor. Indeed, simply photocopying and sharing laws and directives can act as a shield and weapon. The subaltern classes have discovered a powerful means of unifying their actions, morale, and sense of just cause, whilst avoid the repressive measures traditionally associated with dissidence and rebellion.³⁰

Yu reports that workers at the Tonghua Iron and Steel went on strike against a takeover bid by the privately owned Jianlong Steel Holding Company in 2009. 'On July 24, 2009 Tonghua Iron and Steel had a strike [during which] the general manager was killed. Afterwards, [workers] in old state-owned enterprises in many places came up with slogans. One of them was "When the Tonghua Big Boss is doing [bad] things, what should one do about it?" This scared a lot of bosses at state-owned factories that were being restructured so much that they didn't show up for work. Why? They were afraid of being killed.' ³¹

Surprisingly perhaps, popular opinion appeared to consider the killing of the boss to be justified. The incident was widely seen as indicative of proletarian anger and popular resentment. One consequence of the strike was that the Jilin State-owned Assets Supervision and Administration Commission (SASAC) cancelled privatisation. Zhang Wangcheng, a professor of the China Labour Studies Centre at Beijing Normal University, blamed the trade union for the failure to pre-empt the unrest and reduce tensions.³² A month later the ACFTU published a statement that privatisations are illegal unless agreed by the workers' congress.³³

When a strike broke out on May 17th 2010 at Honda's components factory in Foshan, it began as a dispute about low salaries, soon some 1800 workers joined in. They proactively demanded wage rises, new pay scales and career structures, and democratized their workplace union representation. This brought to a head the need for unions to be controlled by the workers themselves.³⁴ The ACFTU leadership nationally announced that democratic elections would replace the appointment of union officials from above, 'step by step', which seems to endorse the Honda workers' ideas.³⁵

An appeal by the strikers indicates the development of a national workers' consciousness. 'Our struggle for rights is not a struggle to protect the mere interests of 1800 workers. We are concerned with the

rights and interests of the workers in the whole country. We want to demonstrate a good example of the struggle for rights of workers.’³⁶

The strike lasted for 17 days and involved 1,800 workers who initially raised over 100 demands including a pay rise of 800 yuan a month and the democratic election of workplace union representatives. The management tried to intimidate the workers and local trade union officials attempted to subvert the strike. The intervention of Zeng Qinghong tipped the balance. Zeng is the CEO of Honda's (50% state owned) joint-venture partner and a member of the National People's Congress. He encouraged the workers to elect their representatives in his presence. They issued an appeal stating that their strike was for the wider interest of workers throughout the country. The company backtracked and initiated departmental workers elections. Negotiations drew in the local government, the enterprise union chairperson, the workers' delegates, Chang Kai, a sympathetic labour professor from Beijing, and Zeng Qinghong. A wage rise of 500 yuan (32.4%) for ordinary workers and of 600 yuan (70%) for student interns was agreed.

In the immediate aftermath of the Honda strike a wave of similar disputes broke out in factories across China, but were most common in Guangdong province. In order to regulate and control these spontaneous outbursts, the Guangdong Province People's Congress discussed a new law, the *'Regulations on the Democratic Management of Enterprises'*. The proposed regulations envisaged a significant extension of workers rights, for example, if 20% of workers in any enterprise demand an increase in wages, the workers would have the right to elect their own representatives to negotiate with management. In the event of their demands being ignored the workers would be able to strike, and the management would not be able to sack them.³⁷ The proposals also envisaged that workers would be guaranteed a one third representation on the board of directors and be able to negotiate on a wide range of issues. Hong Kong manufacturers claim to have successfully lobbied Beijing to shelve these proposals, warning that giving workers a say in

management will provoke ‘endless fights in the boardroom’ because ‘employers want to pay less and employees want to get paid more’.³⁸

After the Honda strike there were no reprisals against worker activists, but the area trade unions manoeuvred to weaken representation of more militant workers. Nevertheless at negotiations one year later, the workers also won big wage rises. The Shenzhen Federation of Trade Unions (SFTU) responded to this challenge of workers’ militancy by initiating direct elections in 163 workplaces with over 1000 workers (Chan, 2013, pp. 129–130). However, student activists took jobs at five factories that were declared to have model trade unions and discovered multiple breaches of the Labour Law and minimal sporadic engagement between the union and the workforce. This, despite numerous encouraging statements from Wang Tongxin the vice-chairperson of the SFTU promoting democratic trade union representation.³⁹

Yu Jianrong notes that the strike participants were mainly born in the 80s and 90s, and in a break from the pattern in recent years: “They were not only protecting existing rights, but were seeking to expand their rights. This indicates a new phase in the rights defence movement of the new generation of wage labourers, which may hasten the birth of a new workers’ rights movement.” (Yu, 2014a, pp. 86–87)

6.10. Social unrest and the CCP’s pursuit of stability

‘The CCP’s historical ideology and legitimacy declares that the “workers are the ruling class” and “peasants are allies” (of the ruling class). Yet, the capitalists’ status has been raised far more in the past decades of reform. The nation is entering a stage of being a well-off society while hundreds of millions of peasants and workers cannot make ends meet. This gap between reality and professed ideology will inevitably shake the political root of the CCP’s ideology and stability of its rule. Avoiding the escalation of social conflict will require, at a minimum, a better protection of the fundamental rights and interests of all citizens, particularly workers and peasants.’ (Yu, 2007, pp. 13–14)

A study by Yongshun Cai into collective labour unrest against factory closures and job losses in SOEs, revealed that protests were led by people from the following backgrounds, 29.2% previous enterprise leaders, 22% party-member workers, 17% current enterprise leaders, 9.8% military veterans, 22% others. In other words sections of the CCP and state bureaucracy led the majority of such disputes (Cai, 2006, pp. 107–108).

Similarly, Yu Jianrong's research indicates that a layer of people with internal knowledge and experience of the system often constitute the unifying force which galvanizes and expresses social unrest: 'The foundations for mass social movement in China may already be laid as there are indications that workers, peasants and the lower class of intellectuals are forging a common identity. Up to this point, workers and peasants have not yet merged into one coherent social group, even though they share a common social status and interests. The formation of their common identity and goals may require an outside group that can act as the bond to bring workers and peasants together. This group could be the 20 million demobilized and retired soldiers living in rural China, which possesses the social capital, organizational, networking and mobilization capabilities to be the bridge between workers and peasants.

'They have already been prominently contributing to peasants' movement to reduce tax burdens and protect land rights. In some southern regions, demobilized and retired soldiers have launched movements to mobilize both workers and peasants. For example, in some regions in Hunan Province, demobilized and retired soldiers built a 100,000-person 'anti-corruption brigade' that was mainly comprised of laid-off workers, poor peasants and lower class intellectuals. In fact, corruption may be the one factor that could bring workers and peasants together since both see this as the root cause of their current predicament and misery. In all past and current social conflicts that involve a combination of workers and peasants, their demands have universally held up anti-corruption (*sic*) as the common enemy.' (Yu, 2007, p. 11)

Yu found that 60% of outbreaks of rural unrest revolve around violations of peasant land rights and 80% of all protests nationwide are defensive conflicts. In other words, Yu believes that they can be resolved with money. By default he maintains that the CCP's designation of such economic conflicts as "contradictions among the people" is correct as they do not threaten the system of power itself.

He suggests that granting land tenure would be the best means to alleviate the pressure of persistent outbreaks of rural discontent (Yu, 2014b).

Whilst Yu believes that China's overall system is stable, he qualifies this designation as one of 'rigid stability'. It is based on those in power dividing up the spoils. This means that unrest rapidly escalates into a challenge to their power. Yu advocates reform to establish a system of 'resilient stability' based on a fair and impartial distribution of wealth, democratic empowerment and popular control over People's Congresses at the country level, and judicial reform to institutionalize procedures and establish the rule of law (Yu, 2014a).

The existing system relies on agencies of surveillance and repression and on pressure relief outlets, like the petitioning system, which allows aggrieved citizens to petition high-levels of government. However, this channel encourages bolder and more determined petitioners to target higher-level authorities as soon as they can, and to mobilize people to increase the pressure. The flip side of this is that local governments accused of wrongdoing often try to hinder petitioners from taking their protests up the hierarchical ladder. Cases of petitioners being dispatched to mental asylums, being detained by local police, and of their petitions being deregistered by means of bribery, have been commonplace (Yu, 2014c).

Stability maintenance known, as *wenwen* is one of the highest priorities of the Party and it encompasses a vast range of state institutions from the pinnacle of power down to neighbourhood and village level committees. It consumes much of the domestic security budget said to be US \$25.6bn

in 2016.⁴⁰ However, stability maintenance activities are so all encompassing that they draw on funds and personnel from a very wide range of state and party agencies as well as from SOEs and private sector enterprises (Chen, 2013, p. 61)

One of the central characteristics of the wenwen system is the willingness of state agencies to spend inordinate sums on containing perceived threats posed by determined activists. This can entail repressive measures; or it can involve official agencies going out of their way to pacify and resolve conflicts. Chen cites an example when relatives of someone killed in a traffic accident in Hubei Province were unable to secure adequate compensation they launched protests to pressure the police. Police officials found them a lawyer and police funds were used to pay the family, and this even involved a collection from officers. Such conciliatory state and party actions tend to encourage copycat displays of militancy. Stipulations restricting the use of legitimate force hamper local officials seeking to contain unrest, so they often turn to underhand methods, underworld gangs etc., as a means of bypassing official procedures. However, it is also common for judicial organs to bend the rules to the benefit of more militant protestors (Chen, 2013, pp. 62–63).

This rigid form of stability is identified by Yu Jianrong as a fragile system particularly when confronted by social unrest. Those in power view protest action as a destabilizing threat to their power, which is seen as a zero sum game, wherein instability poses a threat to those who hold power. As the core of stability policy is containing unrest. It is a system for the management of unrest after it breaks out, rather than a preventative one. When unrest does break out everything is done to secure a resolution. The pressure on officials to contain instability occupies much of their time and energy. And the complexity of many issues that arise is often beyond the capacities of local officials to resolve. Such officials may be stuck in a position where they can't satisfy their superiors and can't control the anger of the lower classes (Yu, 2014a, pp. 88–89).

Yu captures the dynamics between upper and lower levels of the Party and state and wider society succinctly, with a phrase, 'the central government pressures the local government, the local government pressures the people, and the people pressure the central government' (Yu, 2014a, p. 90).

Studies of workers' unrest point to the economic nature of most disputes. Yu notes that common forms of workers' unrest include petitioning higher levels of government, sit-ins, strikes, demonstrations, and blocking traffic. In order to deflect from allegations of illegal assembly and action, protestors often employ innovative and comical methods when negotiating with police or other authorities. For example, to avoid the consequences of being accused of organising illegal demonstrations and marches, such events occur under the auspices of 'taking a walk' or 'going sightseeing'. Legal rights are often used to frame the demands of protests but the legal framework also hinders workers' action, as channels of legitimate expression are ineffective, and local state agencies may collude with employers. However, when put in a corner agencies of the state often grant wholesale concessions.⁴¹

The issue of corruption took centre stage when Xi Jinping became the party's General Secretary of the CCP and the country's president in 2012.

For Yu these patterns reveal the urgent need to take active measures to enforce constitutional legal rights as what he calls *the baseline of social stability*. He views a system based on legal rights as being superior to 'rigid stability', centred around the state monopoly of violence, ideology, and controls on societal organizations.

Workers' conflict plays an important role in influencing party and state policies. However, the nature of long-term policy initiatives that enhanced workers rights, such as the 2008 Labour Law, and the introduction of the right to form democratic workers' congresses in all workplaces - private

and state, - in the Shanghai municipality in 2011⁴² are not simply reactions to immediate threats.

Nor can such measures simply be dismissed as remnants of Maoist rhetoric or trickery, rather they constitute contemporary attempts by party and state agencies to construct mechanisms to channel and contain workers' discontent. These laws and regulations are couched in terms drawn from the dictionary of democratic workers' self-management - a trend that Kornai describes as being wholly socialist in origin (Kornai, 2007, pp. 461–463). Some scholars of China's workers' movements have noted examples of workers' protests that revolved around official legislative structures for workers' management (Xiaoyang and Chan, 2005; Phillion, 2009).

6.10.1. Perspectives on workers' associational power

Walder presents an image of the CCP's state creating a working class from 1949 to 1979. This provides a useful framework to consider the structural formation of production, the working class and state organisation. However, in Walder's work the workers are mainly seen as passive objects of manipulation rather than active or reactive participants or historical protagonists. The Marxist historical school associated with E.P Thompson informs Xing's (2011) sophisticated assessment of China's working class as a 'class-for-itself'. Xing investigates the way that contemporary struggles and consciousness assume a variety of forms that invoke Maoist language and believes that this historical workers' culture expresses a positive identification with the ideals, experiences and struggles, that took place under the Maoist form of socialism. These forms affect workers' consciousness in various ways, shaping their attitudes to concepts like: 'workers are the masters of the state'; collectivism; egalitarianism; and their perception of fundamental categories such as capitalism and socialism.

Xing finds that Chinese workers' invocation of Maoist phraseology is neither nostalgic nor tactical but forms part of the core identity of their subjective consciousness, expressing itself in their communications and culture. Lee argues that workers' struggles are primarily rights struggles rather than class struggles, which, when invoked, are simply fading reflections from the socialist past (Lee, 2007). However, the CCP claims its legitimacy based on its revolutionary heritage. 'The memory of the revolution and Maoist socialism has become an ideological and cultural resource for class- consciousness and the recomposition of the Chinese working class in the post socialist transformation' (Xing, 2011, p. 23).

The forms that workers' communications take: in song; poetry; and in the popular reaction by millions on the Internet to issues dear to the workers hearts, present evidence to back up Xing's theory. Xing points to the development of Hyde Park, Speakers' Corner type centres of debate: on socialism, capitalism and reform, in locations previously designated as

workers' cultural palaces. These debates are dominated by a broadly Maoist framework and language. Xing takes the view that this consciousness is a real factor defining struggles of the workers and perspectives for a future democratic socialist transformation in China.

6.11. Conclusion

China's class structure is unique in the history of socialist states and it has understandably come in for criticism from opponents of capitalism.

To help interpret the character of contemporary class relations in China, I re-examine Kornai's concept of soft-budget constraints. I relate this to his idea that the dilution of socialist ideology and the loosening of the system's internal coherence under reform socialism can strengthen the hand of the workers. This is particularly, but not exclusively, true within public enterprises and institutions at the commanding heights of the economy.

The soft-budget constraint is not only a category of economic inefficiency; it emerges spontaneously from social relations in production between the working class, the party and the bureaucracy. It expresses multiple forms of pressure that the workers are able to exert on the bureaucracy at a micro and macro level. But it also corresponds with the internal motives of the bureaucracy. SBC is ingrained in the relationship between the bureaucracy and the workers, and represents one of the fundamental characteristics of Kornai's theory of reform socialism. As such, SBC plays a central role in defining the actions and behaviour of the bureaucracy and the party.

Wright's theory of class power employs concepts that evaluate the structural position of the workers in the productive system, and the forms of associational power that they can bring to bear within a system. His concept of a triangle of power between the workers, the capitalists and the state, offers a useful framework to evaluate China's class system. The CCP state created China's working class between 1949 and 1981,

and continues to claim that it rules on their behalf. As a consequence, the legal and moral structure of state power continues to derive its legitimacy, vis-à-vis the workers, from its 'communist' and 'socialist' self-identity. The proliferation of capitalist enterprises generated a new working class in the reform era. Policies designed to harden budget constraints and discipline the workforce in the state sector have been promoted and implemented on numerous occasions since the 1980s.

The immense growth of the migrant labour force was exploited by indigenous and foreign private enterprises to create pliant workers with few rights. These enterprises encircle state enterprises and operate under conditions of hard budget constraints. So, under the pressure of market discipline, many state enterprises were closed, sold off, or restructured. However, the reformed state enterprises not only survived, they improved their operations, increased their workforce, and sealed their dominance over the economy by means of their semi-monopolistic status, backed by government support through easy credit. Tens of millions of workers were laid off between 1998-2001 but in direct contrast to the laws of supply and demand, urban wages rose rapidly, regardless of the dramatic spike in unemployment that occurred. Similarly, when the Great Recession hit China and the world economy in 2008, another spike in unemployment, emanated from the private sector. It was during this time that the state introduced labour legislation, which represented a significant improvement in the rights of workers. These moves were synchronized with an immense unionization drive, which anchors and extends the role of official trade unions within all types of enterprises. This represents a means to extend the influence of the party and the state into the private sector and to ameliorate and contain workers' discontent within official institutions and structures. Similarly, the recent introduction of legislation extending the rights of Staff and Workers' Representative Councils to veto managerial decisions can probably best be understood as a means to pre-emptively contain spontaneous outbursts of unrest, by channeling their focus into institutional forms dominated by Party officials. This process to contain unrest is also manifest in the focus of the CCP leadership on maintaining social

stability, which Yu Jianrong has brilliantly described as a system of rigid stability, in which the dynamics of national-local bureaucratic power relations are shaped by the need to respond to outbursts of social unrest.

¹ Wright also notes that associational power could also assume a reactionary form, citing the Iranian revolution.

² Erik Olin Wright *Taking the Social in Socialism Seriously* 2004, p. 5
<https://www.ssc.wisc.edu/~wright/Socialism.pdf> Accessed 11 Dec 2017

³ (Lu, 2012) p.403

⁴ <https://www.bloomberg.com/news/articles/2014-09-15/almost-half-of-chinas-rich-want-to-emigrate>
Accessed 10 Oct 2017

⁵ State enterprises sold housing to their workers at knock down prices at the turn of the century.

⁶ <http://www.stats.gov.cn/tjsj/ndsj/2014/zk/html/Z0402E.htm> Accessed 16.50 GMT 21 May 2015

⁷ Ibid.

⁸ Ibid.

⁹ The scissors was a term that came from the Soviet Union in the 1920s. It referred to falling prices for food and rising prices of manufactured goods.

¹⁰ In this period most TVE's were de-facto private companies, what Huang (2008) saw as the mainstay of Chinese capitalism but after 1989 private finance to TVEs was squeezed and they came back under local government control.

¹¹ The nature of such firms is contested. They can be seen as state enterprises clothed as private enterprises, which function as government agencies operating within soft-budget constraints. This can be applied to most Limited Liability Corporations and Share Holding Corporations in China and to some extent to Joint Ventures. See Huang, Y. (2008). *Capitalism with Chinese characteristics : entrepreneurship and the state*. Cambridge; New York, Cambridge University Press.

¹² The data comes from China's National Bureau of Statistics

<http://www.stats.gov.cn/tjsj/ndsj/2012/html/E0402e.xls>

¹³ There were 120,000 annual deaths from occupational related injuries in China reported in this 2008 World Health Organization report (Wang et al., 2008, p. 1771). 'Injury-related fatalities in China: an under-recognised public-health problem.'

¹⁴ Source National Bureau of Statistics. <http://www.stats.gov.cn/tjsj/ndsj/2013/html/Z0411E.HTM>
Accessed 20 May 2016.

¹⁵ (Hishida, 2010, pp. 1–24)

¹⁶ (Feng Chen, 2009, p. 671)

¹⁷ (Zheng, 2012, p. 290)

¹⁸ For example in the first quarter of 2008 workers won 80% of arbitration cases in Shanghai. Feng Chen (2009). 'Union Power in China Source, Operation, and Constraints.' *Modern China* 35(6): 662-689.
P 672

¹⁹ http://www.chinalawblog.com/2011/04/avoid_china_labor_arbitration_its_a_suckers_game_and_you_will_be_the_sucker.html Published 11 April 2011 Accessed 28 Oct 2013

²⁰ <http://english.acftu.org/template/10002/file.jsp?cid=23&aid=628> (Accessed 23 Oct 2013)

²¹ <http://english.peopledaily.com.cn/90882/8422756.html> (Accessed 23 Oct 2013)

²² Jian Qiao Between the party-state, employers and workers: Multiple roles of the Chinese trade union during market transition-A survey of 1,811 enterprise union chairpersons, p57-8 in Chinese Trade Unions-How Autonomous Are They? Hishida et al 2010 Routledge Oxon

²³ Hu Yaobang's tolerance of student protests in 1986-7 led to him being pressured to resign as General Secretary and make self-criticism.

²⁴ 520,000 labour arbitration cases were registered in 2008, 50% more than 2007

²⁵ This reform socialism is characterized by: the Communist Party's monopoly of political power; public ownership of the commanding heights of the economy; and bureaucratic dominance over society and the legal organizations operating within it. However, reforms permit greater market influence; weaken bureaucratic controls over information and organization, and undermine ideological unity.

²⁶ <http://english.peopledaily.com.cn/constitution/constitution.html>

²⁷ <http://gh.eastday.com/renda/node5902/node5908/node6573/u1a1729811.html> Accessed 13 Dec 2013

²⁸ http://www.bjreview.com.cn/nation/txt/2013-08/05/content_559150.htm

²⁹ Yu Jianrong on "Maintaining a Baseline of Social Stability" Speech to Beijing Lawyers Association on December 26, 2009 <http://chinastudygroup.net/2010/04/you-jianrong-on-maintaining-a-baseline-of-social-stability/> Accessed Oct 23rd 15.04 GMT

³⁰ Yu Jianrong Op. cit. "Maintaining a Baseline of Social Stability" 2009

³¹ <http://chinadigitaltimes.net/2010/03/you-jianrong-%E4%BA%8E%E5%BB%BA%E5%B5%98-maintaining-a-baseline-of-social-stability-part-3/> Accessed 27 April 2015 15.21

³² Finger-pointing in steel mill death 2009-07-29 01:14:59 GMT 2009-07-29 09:14:59 (Beijing Time) Global Times <http://english.sina.com/china/2009/0728/259013.html> Accessed 20 Oct 2010 15.25 GMT

³³ Heed workers' voices (China Daily 08/19/2009 p8) http://www.chinadaily.com.cn/opinion/2009-08/19/content_8586011.htm

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- ³⁴ Anita Chan 2010-06-18 China Daily Labor unrest and role of unions
http://www.chinadaily.com.cn/opinion/2010-06/18/content_9987347_2.htm Accessed 20th Oct 2010 12.40 GMT
- ³⁵ More union heads to face election By Chen Xin (China Daily) 2010-08-31 08:02
http://www.chinadaily.com.cn/china/2010-08/31/content_11228956.htm
- ³⁶ Open Letter to the Public and All the Workers in Honda Auto Parts Manufacturing Co. from the Delegation of Representatives of the Strike Workers for Negotiation. China Study Group 3 June 2010
<http://chinastudygroup.net/2010/06/open-letter-to-the-public-and-all-the-workers-in-honda-auto-parts-manufacturing-co/>
- ³⁷ CLB's analysis of Guangdong's Regulations on the Democratic Management of Enterprises
<http://www.clb.org.hk/en/node/100849> 9 Aug 2010
- ³⁸ Denise Tsang South China Morning Post (Hong Kong)-September 21, 2010 SCMP Morning Edition p1 HK factory owners stifle labour reforms Factory owners stifle labour reforms
- ³⁹ "Power to the Workers" a report by Students on direct elections in Shenzhen
<http://www.clb.org.hk/en/sites/default/files/Image/general/Chinese%20Student%20Trade%20Union%20Report%202013.pdf> Accessed 22:03 5 June 2015.
- ⁴⁰ Finance ministry statement reported in <http://www.rfa.org/english/news/china/china-security-03082016144158.html> Accessed 20 Sept 2017
- ⁴¹ <http://chinadigitaltimes.net/2010/03/you-jianrong-%E4%B8%BE%E5%BB%BA%E5%B5%98-maintaining-a-baseline-of-social-stability-part-3/> Accessed 27 April 2015 15.21
- ⁴² The Shanghai Municipality adopted Regulations on Workers' Congresses in 2010, which became law in 2011. <http://gh.eastday.com/renda/node5902/node5908/node6573/u1a1729811.html>

7. Conclusion: Is China still socialist?

- 7.1. What is the significance for Kornai's theory if China is still socialist?
- 7.2. What about the workers?
- 7.3. What relevance does Preobrazhensky's theory have for studying China?
- 7.4 Questions for a future research agenda
- 7.5 How can Preobrazhensky's ideas be combined with Kornai's theory of socialism?

This thesis addresses the question of whether China is still socialist. To answer this question János Kornai's theory of socialism acts as my primary reference point. His theory is deeply influential in the field of the political economy of socialism, and played an important role in top-level academic and policy debates on reform in Eastern Europe and China.

I believe that socialists should welcome the research and insights offered by János Kornai in his book the Socialist System. Its overview of the basic social and economic regularities of a bureaucratic socialist state offers profound insight into the socialist systems that held power over a third of humanity in the second half of the twentieth century.

Kornai believes that the encirclement of the Chinese Communist Party's economic base by capitalist enterprises, and the internal corruption of party cadres, has produced a system whose outer shell resembles a socialist system, but whose inner nature is defined by its interpenetration with capitalist interests, which produced a qualitative transformation into capitalism (3.3). By contrast, I show that China conforms to Kornai's own definition of socialism.

The categories that Kornai uses to define socialism have a systematic, coherent, and logical structure. He employs three primary definitions.

1. Rule by a Communist Party that is hostile to private property.
2. Public ownership of the commanding heights of the economy.
3. Bureaucratic coordination of the economy by means of planning.

In addition, he identifies a number of secondary features and tendencies, which appear with regularity in those societies that are based on the

above three characteristics of socialism (2.4.1-2.4.3)

Of these secondary features of socialism, I focus attention on the dynamics of forced growth (2.3.3.1), socialist economic cycles (2.4.3.2), vertical dependence (2.6.1), soft budget constraints (2.6.2), and market socialism (2.5.2).

Kornai's method of categorization and analysis of socialist states is rooted in his observation of systems that ruled over a third of humanity in the 20th century. During his intellectual voyage from being an advocate of Marxism to become a supporter of capitalism, he developed his systems theory. This approach originates from the Marxist method employed in the analysis of capitalism as a whole, and to study socialist systems in the 20th century as a totality.

In order to verify if China fits Kornai's definition of socialism, I draw on specialist English language literature and scholarship on Chinese economics, politics, and class relations. However, no previous scholars have attempted a detailed assessment of this literature with the express intention of comparing China to Kornai's theory of socialism. Where statistics are relied on to clarify ownership relations, for example in Limited Liability Companies and Shareholding enterprises (3.7-3.7.2), it must be conceded that the data may suffer from deliberate and accidental attempts to conceal the facts. This may serve as a means of protecting interest groups and individuals from critical scrutiny or even criminal charges. This is a particularly important phenomenon in contemporary China, where the scope of Xi Jinping's anti-corruption campaign has generated a widespread sense of fear within bureaucratic administrative circles at the upper and lower levels of the Party and state (3.9). However, to mitigate the risks of relying on potentially misleading data, I draw on analysis and research from leading China scholars with scrupulous credentials for accuracy who are widely recognized by academics in the field (Dickson, 2011; Bruce J Dickson, 2014; Goodman, 2014; Heilmann, 2017; Heilmann and Melton, 2013; Huang, 2008; Lin et al., 2003; Lin, 2012; Naughton, 1996, 2013, 2017; Oi and Walter, 2011; Shambaugh, 2016, 2008; Walder, 1984; Andrew G Walder, 2004;

Walder, 2011b; Xu, 2011, 2017)

I believe that Kornai's approach, whose central focus is on the evaluation of the social relations of power in the context of the socialist system, is broadly correct. It draws special attention to the Party's exclusive control, the bureaucratic hierarchy, the appointment system, social organizations, the mass media, the education system etc., in other words, to the full panoply of its instruments of power (3.4-3.8).

Nevertheless, it must be conceded that although China's system provides a very close match with Kornai's theory of socialist systems, this match stretches the parameters of his original concept to incorporate elements that were certainly not part of the experience of socialism before 1989, e.g. there were no billionaires (4.2), and although private businesses existed in reform socialist countries, the size, scale, quantity and quality (4.10.1) of private business operating in China today, dwarfs anything that existed in Hungary, Poland, Yugoslavia, or in China itself before 1989.

7.1. What is the significance for Kornai's theory if China is still socialist?

Kornai's foray into the study of capitalism as a system (4.11) puts its main emphasis on one feature; the "surplus economy". He defines this as a "system specific feature" of capitalism, and the "shortage economy" as a system specific feature of socialism. However, although Kornai previously employed these categories as systemic features in his earlier work on socialism, they were relegated to secondary and subordinate role, and so, were not used to define the system.

The problem with his new approach is twofold.

1. It risks undermining the internal coherence of Kornai's general theory of socialism.
2. If, as I contend, China's three core systemic features correspond with Kornai's original theory of reform socialism, then either the phenomenon of a surplus economy is compatible with socialism, or China's system

shows that capitalism can also be based on the three basic foundations of socialism.

Xu Chenggang who is a close collaborator with Kornai, attempts to resolve Kornai's dilemma by identifying China's system as a Leninist form of "state capitalism," similar to the New Economic Policy (NEP) in the Soviet Union during the 1920s (4.11). Whilst I concur with Xu's view that the Chinese system displays core features that resemble the NEP, I find that his employment of the term "state capitalism" conceals more than it explains. State capitalism under Lenin was the use of capitalist methods to improve the economy of the socialist state. Indeed, Kornai identifies the Soviet Union in the 1920s as a "revolutionary transitional system" and views Leninism as the original prototype of all future socialist states (2.3).

In Kornai's view the central political difference between capitalism and socialism is that while socialism and capitalism can both be dictatorial political systems, socialism can never be democratic (Kornai, 2016, p. 569). However, if, as Kornai holds, China is already capitalist, then there is *no objective hindrance to China becoming democratic*. Then the hypothetical question arises, what if China's system were to become democratic and yet simultaneously retain a dominant role for the state economy? And what if outbursts of discontent find expression in demands for a democratic form of socialism? Kornai categorically excludes the combination of socialism with democracy. His justification for this assessment is based on the experience of real socialist states but this clearly contains a powerful normative element.

If public ownership of the commanding heights and a dominant role for planning are, at least potentially, neutral systemic features, this signifies that the degree of hostility or tolerance towards private property by the ruling political power is the quality that defines a system as either socialist or capitalist. Then, when public ownership of the commanding heights and planned coordination predominate, the choice of socialism or capitalism is simply a subjective decision made by political leaders. If so,

there is nothing socialist about the combination of public ownership of the commanding heights and planned coordination of the economy. If changing system is a purely subjective choice, then selecting between socialism and capitalism is a capricious affair. However, if the property forms of each system are aligned with specific class and bureaucratic interests, then even the most determined attempt to change to or from a socialist system may encounter stiff or insurmountable resistance.

I think this goes some way to explain why declarations and resolutions, like the decision of the Third Plenum in 2013 that championed markets and private sector interests in China are thwarted by a coalition of bureaucratic interests (3.8). Similarly, in capitalist democracies, Social Democratic parties that are elected on a popular mandate to elevate public interest and public property above capitalist interests, meet stiff resistance from forces defending capitalism.

Indeed, Kornai interprets the mass unrest in China in 1989 as an expression of *popular antipathy against capitalist reforms* (6.9.1)

‘The man in the street ...lumps together higher earnings earned by real merit with those accruing from privileges of power, and market profits with the ill-gotten gains of corruption. A surge of hatred for ‘speculators’ and ‘corruption’ breaks out. That was one factor influencing the atmosphere of the 1989 student demonstrations in China. Stuck halfway, the reform process digs the ground from under its own feet, alienating a sizable section of the general public.’ (Kornai, 2007, p. 510 [1992])

7.2. What about the workers?

The Chinese Communist Party (CCP) established liberated zones from 1929 onwards. It designed and exercised local state power in these areas until 1949. These are the earliest and most enduring examples of isolated statelets ruled by a Communist party and its guerrilla army (6.3.1). After 1949, all state power passed to the CCP, and its organs of exclusive power penetrated into every institution, community and family.

The economic foundation of the system was state-ownership of the commanding heights. This political-legal ownership form is also the economic foundation of socialism according to Kornai and Preobrazhensky. The official ideology continues to operate within the terms of reference of communism and socialism and this ideology is not accidental (3.4 and 3.7.4). Rather, I believe it is embedded in the specific historical relation of forces between various classes and interests as Rothenberg suggests (6.5) and I attempt to show this in relation to social unrest ((6.9.2 - 6.10.1). I show that bureaucratic power emanates from the vast panoply of the CCPs interwoven agencies of control and organisation over society (3.5-3.8).

Although Kornai excludes the possibility of combining socialism and democracy, he nevertheless points to self-management as a democratic socialist tendency that recurrently finds expression in socialist countries (2.5.3). The reason why this trend emerges repeatedly in socialist states is rooted in the contradictions between communist ideology and the reality of workers' conditions. These contradictions are inherent to the nature of socialist systems. In addition, in those socialist countries which experienced a long-term labour shortage, Kornai notes that this generates workplace relations where:

'It was generally realized how much this circumstance weakened labor's discipline. Employees justifiably felt they would not be dismissed even if they did not try very hard, or even if they shirked entirely. If they were dismissed, they could easily find other employment. All managers and supervisors continually complained of this. Many of the workers did their work properly out of an underlying sense of honesty and identification with the job, and in some places where it could be done effectively, they might be rewarded for this financially. But they were not haunted by the disciplinary specter of unemployment. The situation, let us admit, had some advantages for the employees.' (Kornai, 2014, p. 104)

It is with this feature of Kornai's theory of socialism in mind that chapter 6

considers class and labour relations in China. In particular, it looks at how the identity of the party and state, which claims to be the expression of the world historical interests of the proletariat, affects the character of social and class struggles, and the responses by different levels in the party to them. For example, the legitimacy of the CCP rests on its claim to incarnate the workers' interests. Thus, examples of demands from the workers to veto enterprise management decisions and to democratize trade union elections, particularly in state owned or state controlled enterprises are recurrent features in China. Indeed, I would go so far as to say that there exists a particular set of economic, political and class relations between the Communist Party and the working class within socialist systems, which merits classification within Kornai's system as a specific feature of socialism (see parts 6.9.2. and 6.10.).

Kornai attributes those advantages that accrue to workers in socialist systems to the persistent tendency to labour shortage. This phenomenon also finds expression in system specific types of workers' unrest, e.g. protests, strikes, and other forms of resistance, that break out in socialist states. Indeed, "self-management" tendencies are one of the ways that the party and bureaucracy reflect and respond to such forms of unrest.

A related phenomenon in Kornai's theory is the soft budget constraint (see parts 2.6. and 6.2.). This is rooted in the structure of social and class relations and expresses pressure at the enterprise level, at an industry wide level, and through pressure on urban authorities to satisfy the needs of the masses. It expresses a myriad of ways that the working class and the peasantry are able to exert pressure on lower and upper-levels of the party and bureaucracy to protect jobs, and expand social and welfare rights. This integrates concepts of class and class struggle into an assessment of the contradictions driving and shaping the character of party and state power in China, and it informs my analysis of Chinese society today.

The reform era witnessed a colossal expansion in the size of the working class. This was based on a process of urbanization and the growth of rural industry. It simultaneously undermined and transformed the position of urban workers

within the state sector. These workers previously enjoyed a highly privileged position in comparison with non-state workers and with the rural population. The Maoist concord between the Party and the urban proletariat elevated their designated social position to the 'leading class' and the 'masters of the state'. However, the balance of forces anchored in the Maoist era was based on the near total prohibition against migration from the country to the cities.

I believe that the character of social unrest in China often appears as a self-management tendency. And this corresponds to a wide variety of the Chinese protest forms that Yu Jianrong investigates. Eric Olin Wright's analysis takes statist, associational, and economic power to be three poles corresponding to specific power relations. These are based on bureaucratic interests, like classical Stalinism, free associational relations, such as Marx envisaged in advanced socialism, and capitalist interests, based on exploitation of the working class through the ownership and control of capital. From this perspective self-management can be interpreted as the expression of associational power through its structurally embedded links to statist power, in other words, the ways that CCP and the ACFTU cadres respond to demands of the workers, particularly those working in the commanding heights of the state economy (6.8.2). The socialist objectives of the Party and the trade unions are in conflict with capitalist accumulation and the corruption of Party and ACFTU cadres. So, despite the CCP dictatorship, and draconian forms employment discipline, particularly in private companies, militant unrest is a commonplace. Indeed, the influential role of lower level Party members and cadres, who often support or organize these workers' and peasants' struggles, is well documented (6.10). I maintain that the CCP's claim to represent the interests of the workers and peasants remains central to its legitimacy.¹

7.3. What relevance does Preobrazhensky's theory have for studying China?

In chapter 5 Preobrazhensky's theory of the character of socialist accumulation in a backward country is explained by reference to the

historical circumstances of the NEP (5.3). During this time, the theory was developed and efforts were made to test it against reality. Central to this theory is the idea that economic policy during the transition to socialism is subject to two main laws. The first is the law of primitive socialist accumulation, which seeks to optimize accumulation by the state sector by pumping over resources from private sectors of the economy. The second law is the law of value, which seeks to elevate profit seeking private business interests to the dominant economic regulator of the economy.

For Preobrazhensky the idea that the socialist objectives of policy could be harmoniously and permanently aligned with capitalist objectives was utopian. This is rooted in the concept of a fundamental antagonism between the interests of the working class and the capitalists that constitutes a core axiom of Marxist thought.

However, during the era of primitive socialist accumulation Preobrazhensky envisaged that planning would be based on a mixed economy dominated by public ownership at the commanding heights of the economy. It was not anticipated that the mixed economy would be abolished any time soon. Indeed, the NEP had originally been introduced in the Soviet Union as an antidote to War Communism, in which nationalization and requisition for the war effort, wiped out privately owned enterprises altogether. The NEP encouraged the private economy and market based activity and communists learnt to trade. Preobrazhensky explained through multiple examples how a socialist state could exploit its power over the economy and state to extract resources from the private sector (5.5-5.7.4).

It was Preobrazhensky's view that an optimal policy environment in an economy guided by primitive socialist accumulation would permit a rate of exploitation from the private economy that would constitute a less onerous burden on petty producers than either capitalism or feudalism. If the process ensures that plans worked out in advance for the overall development of the economy are realized; then this shows that planning

based on PSA is the dominant economic regulator. If by contrast the private sector regulates the economy then the vicissitudes of profit seeking enterprises competing for markets will produce a significantly different economic structure, organized by the law of value (5.5.-5.5.3.).

Preobrazhensky's idea of socialism is rooted in Marx's concept of material development, which, on a timeline, locates socialism in the future, when the material foundations for universal abundance are attained or are within reach.

7.4 Questions for a future research agenda

Although I examine China using the lens of Preobrazhensky's conceptual framework, I have not undertaken to provide detailed empirical verification for China's macro-level processes using his method. It is my hope that further research, to master the data on China's economy and society may assist the elaboration of plans, and the avoidance or limitation of crises. This would require more accurate data sets about the forms of ownership and control of the economy in each of the key sectors on a national scale. In this way the transfer of resources between ownership types can more easily be identified and the process of discovering the optimal rate of accumulation could be fine-tuned.

I believe that the following questions emerge from Preobrazhensky's theories, and indicate a future empirical research agenda to help study China's system.

1. What transfers occur between different ownership sectors?
2. How can ownership relations be more precisely defined?
3. What is the extent of illegal bureaucratic accumulation?
4. How can we measure the extent of wealth transferred to the state by rural land transfers?
5. How can the quantity of transfers from peasants who become migrant workers be measured?
6. Do rural collective entities act as collective, state or private

companies?

7. Do patterns of centralization and decentralization correspond with increasing or decreasing state accumulation?
8. How is state accumulation divided between different types of public or semi-public enterprises?
9. To what extent are investments by China's capitalists linked to state planning objectives?
10. To what degree can market impulses be said to shape the economic landscape in China?
11. How effective are state controls over the in and outflow of capital and goods?
12. How influential are party cells inside capitalist enterprises?
13. How do party cells operate to shape policy in each type of ownership sector? To what extent are there differences based on region, sector, etc?
14. To what degree do China's tech giants share their data with state agencies?
15. Are state agencies able to effectively employ the big data resources that they have access to?
16. What is the extent of China's growth that stems from emulation and duplication of inventions and innovation developed by capitalism?
17. How systematic and effective is the planning system in exploiting such emulation and duplication?
18. To what extent is the growth of ACFTU membership fictional? And does the ACFTU constitute a power within workplaces?

7.5 How can Preobrazhensky's ideas be combined with Kornai's theory of socialism?

Preobrazhensky's theory of primitive socialist accumulation originated in the context of the New Economic Policy in the 1920s; this was a system based on state ownership and state monopoly over the commanding heights of the economy, which coexisted with capitalist and petty bourgeois economic sectors.

Preobrazhensky did not engage in a detailed analysis of the rise of bureaucratic planning or how it might amend the principles of primitive socialist accumulation. Indeed, in the 1920s, he regarded bureaucratic degeneration as a phenomenon that could be contained. His principal concern was that capitalist forces might threaten the revolutionary state, leading to the overthrow of the dominance of public property in the commanding heights of the economy, and the dissolution of the state economy.

In a backward socialist economy the optimal rate of socialist accumulation inevitably and unavoidably entails the continued existence of capitalist and pre-capitalist economic forms. By optimal, I refer not to the maximum resources that can be acquired by the state at a given moment i.e. by immediate and universal nationalization but to the medium and long-term process whereby the state economy is able to expand and improve its productive potential through an on-going process of accumulation from pre-socialist economic formations and social relations. This entails a process more akin to harvesting resources from the private sector than expropriating all means of production regardless of size, or the capacity of the state to produce the same goods.

According to my interpretation of Preobazhensky's theory, the coexistence of socialist and pre-socialist forms is an essential prerequisite for optimal accumulation, growth and progress. Indeed, I maintain that the economic constellation, which emerged in the reform era, should not be understood simply as the advance of capitalism and the decay and degeneration of socialist remnants. Instead, during the reform era the continual predominance of public ownership in the commanding heights of the economy combined with the structure of political power and bureaucratic administration automatically generates pressure to contain the advance of capitalism, and to accumulate resources from capitalist and pre-capitalist sectors. From this perspective reform socialism, as understood by Kornai, is not necessarily an incoherent system, destined for revolutionary destruction and internal disintegration, as he believes (see 2.5 to 2.8).

Preobrazhensky's theory understands socialism during the period of PSA as a

system moving towards socialism whilst exploiting capitalist and pre-capitalist economic forms. However, contradictions in this development pattern generate sharp social, economic, and political crises. This results in dramatic changes in policy, mediated through the bureaucratic system of command. These assume the appearance of zigzags in policy between tightening and loosening control, and centralization and decentralization. However, throughout all these phases the enduring characteristics rooted in the system's basic features, maintain their efficacy, influence, and dominance. At the heart of this process of reproduction is the drive towards state accumulation, state investment, and the expansion of the scale, terrain and ambition of party and bureaucratic agencies.

Here a close parallel exists between Preobrazensky's theory of original socialist accumulation and Kornai's concept of forced growth. Forced growth in Kornai's schema expresses the automatic driving forces of a bureaucratically planned and publicly owned economy (2.4.3.1). I believe that the specific characteristics of the Soviet and Chinese experience of accelerated accumulation closely correspond to Kornai's description of forced growth and investment hunger both under classical and reform socialism. This process is seen as the spontaneous product of the combination of state ownership of the commanding heights and bureaucratic coordination.

The main focus of state investment in China is physical infrastructure and the built environment. The tendencies described by Kornai to focus on rapid growth, priority targets, physical infrastructure, and mega-projects are very pronounced in China today (see parts 2.4.3.1 and 3.8-3.10).

The party's planning policies as illustrated in the 12th Five Year Plan determine the pattern of accumulation and economic dynamics. They unify the state monopoly of power with state dominance of the economy to shape society (3.8.1). By contrast capitalism is driven by profit-seeking investment by private enterprises, state power is subordinate to this objective, and the private sector dominates the economy.

The CCP and the state bureaucracy automatically organize their actions in ways that expand their terrain of influence and power. This produces a self-replicating and automatic dynamic – to reproduce the existing correlation of power relations and to shape them, whilst containing social discontent. This process revolves around the fulfilment of state and local planning targets and objectives, which are enforced by the punishment and reward systems for cadres (see 3.8).

I believe that the dominance of state ownership of the commanding heights of the economy, guided by national plan, acts as a *compelling force on China's leaders to act the way they do, or to act within circumstances that they do not and cannot simply shape as they wish*. This generates recurring patterns and contradictions. They take the form of conflicts over bureaucratic administration; workers' and peasants' discontent, planning versus markets, state versus private ownership; political reform versus the repression of 'bourgeois forces'; centralization and decentralization etc. These forms of appearance are the product of social relations, which emerge within an objective environment that fundamentally differs from the socio-economic dynamics of capitalism.

While the clashes between factions and ideologies inside the CCP may appear to be ideologically driven conflicts, I believe that the roles that these actors play are better understood as 'character masks' i.e. as forms of behaviour that correspond to specific class and bureaucratic interests within the system. Marx employed this concept to argue that the actions of people with different class interests tend to adopt an almost theatrical form corresponding to these interests.

China's ideological adjustments throughout the reform era entailed a declining emphasis on planning and an apparent ambivalence to its relative weight within the economy. This also corresponded to the re-emergence of highly exploitative private enterprises, therefore the CCP's linguistic twists and turns have generally been interpreted as a ritualistic and coded language that barely conceal the open embrace of capitalism.

This is commonly lauded by pro-capitalists and condemned by socialists around the world.

However, I believe that the ideological stance of the CCP leadership should not simply be viewed as an inconsistent, contrived, and theatrical ritual, designed to dupe the people. Rather it is an attempt to formulate a theoretical understanding of Chinese society from within its historically embedded reality.

When Kornai writes about reform socialism he tends to present it as a deviation from the *norm* of classical socialism. It is an incoherent and contradictory system and ideology. Eventually, it anchors private ownership and market coordination so deeply in society, that the pressures pushing for a transition to a capitalist market economy overwhelm the old system. This produces a revolutionary transformation, such as we saw between 1989 and 1991 in Eastern Europe and the Soviet Union.

Preobrazhensky's theory of socialist economic development has two distinct advantages compared to Kornai's, which can be usefully employed to examine contemporary China.

1. He assumes that after the socialist revolution there will be a prolonged period during which a socialist state develops its economy whilst the external environment is still capitalist. State-owned enterprises dominate the commanding heights of the economy, but operate where commodity production and capitalist relations are widespread and even growing. Indeed, the socialist state may need to actively encourage capitalist production and markets in order to develop the forces of production and the working class.
2. Preobrazhensky does not assume that socialist planning must inevitably degenerate into a bureaucratic system of power. Whereas Kornai equates socialism with innate dysfunctionality attributable to inexorable bureaucratic tendencies, which the abolition of the dominance of capitalism and free market prices automatically entails.

Preobrazhensky explains that the laws of a planned economy should be governed by regularity and necessity. For example, if a socialist state decides to build a new city of a million inhabitants it has to consciously mobilize the required resources and manpower. In an ideal world, one planning decision connects to another, and becomes unified into a coherent set of actions that create the city, with infrastructure that is fit for purpose. To build the city's roads, houses, shops, etc. requires machinery, equipment and manpower, and the workforce needs food, clothing and shelter etc. Of course, it is possible to build a city by means of planning or markets, and all modern cities are built by some combination of the two. However, in a transitional economy that is supposed to be moving towards socialism, macro-level planning principles – the law of planning based on primitive socialist accumulation - acts as the main driving force building the city.

Indeed, I refer to the building of cities because the process of planned urbanisation in contemporary China has no parallel in any capitalist economy, in terms of its speed and scale, and in the role of planning in driving this process. The party seeks to modernize society through an urbanization drive that creates a new working class composed of hundreds of millions of rural migrants. However, the New Urbanization plan is not market driven. And nothing indicates that capitalist investment for profit would provide work, livelihood and welfare for 100s of millions of new urbanites as envisaged under present policies (see 3.8.2).

The CCP and the bureaucracy continue to exercise a dominant position within China's social structure. Every level of the bureaucracy has connections to wider society and comes under pressure from different class interests. To remain in power they have to mediate these interests and class conflicts whilst administering society. I believe that this constellation ensures that China's ruling party and bureaucracy can force the pace of economic development and modernization through vast megaprojects, which are increasingly international in scope.

¹ An analogous process appears in West European social democratic parties, which rely on support from a working class constituency. Despite repeated and explicit attempts to transform these parties into people's

parties with no specific affinity to the working class, and to jettison their historical association with working class identity and socialist ideology, the embedded relationship between the party and the workers continues to haunt such parties. Indeed, even in the British Labour Party and the German Social-Democrats, which eliminated overt socialist clauses and objectives from their constitutions, the relationship between the workers and the party remains central to their identity.

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